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On the cover
The withdrawal of Harriet Miers's nomination to the Supreme Court is a further blow to an already storm-damaged George Bush: leader

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Politics this week

Oct 27th 2005
From The Economist print edition

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Quake aid

The United Nations raised fresh pledges of $580m for those affected by **Kashmir's earthquake**. Oxfam had accused some rich countries, including France and Finland, of giving nothing. More than 3m people were left homeless by the quake on October 8th. See article

China said 545 chickens and ducks have died of **bird flu** in a village in the central province of Hunan, in the country's third major outbreak of the disease in two weeks.

America and Japan were said to have reached agreement on relocating a controversial air base on the island of **Okinawa**, but the locals may not be satisfied. See article

Prime suspects

An interim UN report pointed an accusing finger at top figures in the Syrian government and intelligence services for the murder of the former Lebanese prime minister, **Rafik Hariri,** last February. America and its allies are threatening sanctions unless Syria complies fully with the rest of the UN investigation. See article

Numerous countries protested to **Iran** after its new president, Mahmoud Ahmadinejad, told a conference entitled “The World without Zionism” that Israel should be “wiped off the map”. Israel's foreign minister, Silvan Shalom, said his country considered Iran “a clear and present danger”.

Mahmoud Abbas, the **Palestinian president**, returned from a trip to Washington disappointed. George Bush ignored his call for immediate talks on Palestinian statehood, and hinted that a state may not emerge before the end of his presidential term. But Mr Bush tacitly supported Hamas's participation in legislative elections next January, and Israel seemed to get the message too. It backtracked on a pledge to prevent the Islamist party from taking part.

Six people died and about 30 were wounded in a **suicide bomb attack** on the Israeli town of Hadera. The Palestinian Islamic Jihad claimed responsibility in revenge for the killing of one of its leaders by Israeli forces. Israel replied with attacks and arrests in the occupied territories.

Iraq said its new constitution had been approved, but only just. Although it received strong support from Kurds and Shia Arabs, the Sunni Arabs only narrowly failed to scupper the whole project; they almost managed to get the required number of no votes in the province of Nineveh. See article

Kizza Besigye, a former presidential candidate, returned to **Uganda** after four years in exile to contest the presidential election next year. He had fled in 2001 claiming his life was in danger. The

government of Yoweri Museveni said he could still be arrested for alleged links to rebel groups.

Tempest-tossed

Reuters

Hurricane Wilma battered Cancún, Mexico's biggest tourist resort, for two days, before flooding Cuba's north-west coast and tearing across Florida. Only eight people were killed in Mexico, but there was widespread damage. In Florida, ten people were killed and up to 6m were left without power. Tropical storm **Alpha**, so named because hurricanes have outpaced the alphabet this year, killed 15 people in Haiti and the Dominican Republic. See article

Argentina's mid-term congressional election gave a mandate to the country's president, Néstor Kirchner, whose candidates won around 40% of the vote. His wife, Cristina Fernández, standing for the senate in Buenos Aires province, convincingly defeated the wife of Eduardo Duhalde, a former president. Mauricio Macri, the conservative president of Boca Juniors football club, won the election for the lower house in the capital. See article

Brazilians voted by 64-36% against a proposed ban on gun sales. **Brazil** has more gunshot deaths per head than any country in the world except Venezuela, according to the United Nations.

America's secretary of state, Condoleezza Rice, visiting Ottawa, called on Canadians to keep “in perspective” a longstanding dispute over trade in **softwood lumber**. The United States has refused to abide by the ruling of a NAFTA tribunal to pay back to Canada $3.5 billion in countervailing duties on lumber.

The White House waits

America waited for Patrick Fitzgerald, the special prosecutor, to say whether or not he was bringing indictments against a number of senior Bush administration officials in the case of the leaking of the identity of **Valerie Plame**, a covert CIA agent. See article

As the **death toll of Americans** in Iraq passed 2,000, President George Bush, in a speech to military spouses, said America's enemies were trying to establish a “totalitarian empire”, and that more sacrifices would be necessary to stop them.

After a four-week trial and 12 years of legal delays, a jury ruled that the Port Authority of New York and New Jersey, the agency that once owned the **World Trade Centre**, was negligent when the building was bombed in 1993.

Harriet Miers, George Bush's latest nominee for the Supreme Court, withdrew her name from consideration. She had been widely attacked for her lack of judicial experience. See article

Poles apart

Reuters

In **Poland's** presidential election, a surprise victory was won by a right-wing populist, Lech Kaczynski, the socially conservative mayor of Warsaw, whose twin brother Jaroslaw led his party to victory in September's general election. The election result threw into confusion

efforts to forge a new governing coalition out of two right-of-centre parties. See article

Tony Blair admitted, as he prepared to host an informal **European Union** summit on globalisation, that there was little hope of making deep cuts in the group's farm spending. But he pledged to do everything he could to settle by December a row with France over the EU budget.

A leading financier in **Bulgaria** was assassinated. The killing of Emil Kyulev was the latest in a series of contract killings whose frequency has upset the European Commission and prompted warnings that the country may not be able to join the European Union as planned in 2007. See article

A **German** court sentenced four Arab men, accused of planning attacks on Jewish targets, to jail terms of between five and eight years. The prosecution described them as the most important members of the German branch of al-Tawhid, an Islamist group said to have links with al-Qaeda.

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Business this week

Oct 27th 2005
From The Economist print edition

Succeeding Mr Greenspan

George Bush nominated **Ben Bernanke**, a leading monetary-policy expert, to replace Alan Greenspan as chairman of the Federal Reserve Board. The nominee is well-known as the current chairman of the White House's Council of Economic Advisers. See article

Market reaction to the Fed nomination was mixed. **Stock prices rose** on Wall Street, with the Dow Industrials index posting its biggest gain in six months. But bonds fell because some feared that Mr Bernanke may not be tough enough on inflation.

Ericsson, a Swedish telecommunications equipment-maker, said it would pay $2 billion to buy most of the assets of **Marconi**, including its network-equipment business. The combination is meant to help Ericsson compete in the booming market for broadband internet equipment and services. Marconi will retain its British services business. More than 1,000 employees could lose their jobs when the two companies combine their business operations. See article

Steel deal

Ukraine agreed to sell its biggest steel mill to Lakshmi Mittal, a steel tycoon, for $4.8 billion. The deal for Kryvorizhstal marks Ukraine's biggest privatisation thus far. It was seen as a victory for President Viktor Yushchenko, who succeeded in reversing an earlier sale of the steel business at a much lower price to a consortium that included the son-in-law of the ex-president Leonid Kuchma. See article

The chief executive of **Wal-Mart** said America's Congress should consider raising the minimum wage. The comments by Lee Scott were seen as an effort by the stores group to soften its image, which has been bruised by charges that it treats employees poorly. See article

India's central bank raised short-term interest rates in a bid to ease inflationary pressure. High oil prices and fast economic growth were both seen as factors in the move. Meanwhile, the central bank put its economic-growth forecast for the year ending March 31st at 7% to 7.5%, an increase on its earlier projection of around 7%. See article

Macquarie Bank of Australia extended an international buying spree with a takeover offer for the firm that owns Copenhagen airport, despite resistance from the Danish government. Macquarie also bought a stake in a cargo port on China's Yangtze river.

Anglo American will restructure and return up to $1 billion to investors next year after selling off business stakes. The giant mining company's plan, which is intended to refocus its operations on its core mining business, includes cutting its 51% stake in AngloGold Ashanti, a gold company.

Santander in America

Seeking a corner in America's consumer-banking market, **Banco Santander Central Hispano** of Spain agreed to pay $2.4 billion for nearly 20% of Sovereign Bancorp of Philadelphia. Santander has an option to buy the entire bank after 2008. Sovereign, in turn, plans to buy a community bank in New York to expand its branch network. The Spanish bank has units elsewhere in Europe and Latin America.

New bidders surfaced expressing interest in the futures arm of **Refco**, a big futures and commodity broker that has filed for bankruptcy, after the withdrawal of an earlier offer from a group led by J.C. Flowers & Co. Creditors and industry leaders called for a quick resolution, before Refco's business suffers further. See article

The Carlyle Group, a large American private-equity firm, agreed to spend $375m for a majority stake in China's biggest machinery company. Carlyle edged out several rivals, including Caterpillar, to strike the deal for Xugong Group Construction Machinery. It is one of the largest private-equity deals in China.

Cendant, an American travel and property giant, unveiled plans to split into four companies next year. The firm, parent of such well-known brands as Orbitz and Ramada, says its future business units will focus on property services, travel, hospitality and vehicle rental.

Growing public concern over **bird flu** is affecting consumption of poultry products in Europe. Britain and Italy, among other countries, have seen sharp falls in demand for poultry. Meanwhile, the European Food Safety Authority has issued a warning against eating raw eggs and called for proper cooking of chicken before it is consumed.

Buoyant burghers

German business sentiment hit a five-year high this month, which spurred hopes for a broad-based recovery in the country's economy. Sentiment in Germany's retail sector showed the strongest improvement, but all sectors surveyed by Ifo, the institute that conducts the business poll, were more optimistic.

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George Bush

Storm damage

Oct 27th 2005
From The Economist print edition

George Bush should use Harriet Miers's withdrawal as a prompt to rebuild his presidency

Get article background

MANY jobs get easier the longer you do them. But not the presidency. The second term usually sees the occupant of the White House gradually engulfed by scandal and disappointment: that was the story with both Ronald Reagan and Bill Clinton. Seldom, however, has the fall from grace been as rapid as it has been with George Bush. The man who marched triumphantly back into the White House a year ago at the head of a conservative revolution now looks more isolated and powerless than ever.

This week, Mr Bush suffered one hefty blow to his authority and prepared to receive another. On October 27th Harriet Miers, his personal lawyer, whom he had foolishly nominated to the Supreme Court, withdrew. The excuse given was that she could not answer the questions asked of her by increasingly indignant senators without breaking rules about client privilege. In fact, her nomination was in trouble with politicians of all persuasions for the simple reason that she was woefully underqualified for the highest court in the land. Even social conservatives objected to a born-again Christian who opposed abortion on the ground that she looked like a presidential crony.

It was also a personal humiliation for Mr Bush. He had vouched for her character. His basic pitch on her behalf had come down to two words: trust me. But many senators were not inclined to do so. They saw a woman with little experience of constitutional law, whose main qualification seemed to be a fawning admiration for “the most brilliant man she had ever met”. Ms Miers's written answers to the Judiciary Committee were so embarrassing that senators from both sides asked her to resubmit them. This was clearly an exercise in nepotism rather than careful selection.

The Plame blame falls maybe on the Brain

The second potential blow, still undelivered as *The Economist* went to press, was due from Patrick Fitzgerald, a special prosecutor investigating the “outing” of a covert CIA agent called Valerie Plame. In his sights were two of the president's men: Karl Rove, Mr Bush's main political adviser (whom Democrats refer to dismissively as “the president's brain”), and Scooter Libby, chief-of-staff to Dick Cheney. There was even a danger of Mr Cheney himself being sucked into part of it.

The case is a complicated one. It revolves around the spin-doctors' briefing of journalists about Ms Plame's husband, Joseph Wilson, a former ambassador, who had been sent to Niger by the CIA to investigate whether Saddam Hussein was trying to buy uranium there—and who had subsequently accused Mr Bush of lying on that score. Much depends on whether Mr Bush's men knew that Ms Plame was a covert agent, and what exactly they said to the investigating prosecutor. All the same, any indictment, even under a technicality to do with perjury, would still be a hammer-blow if it involved Mr Rove. The architect of Mr Bush's victories in 2000 and 2004 is not only crucial to the running of the White House; he is also the man best placed to repair Mr Bush's relations with the right. Conservatives are furious not just about the Miers nomination, but also about government spending and Iraq.

The problem for Mr Bush is that Ms Miers's withdrawal and the fuss about Plamegate compound a picture of incompetence and sleaze. In the wake of his disastrous handling of Hurricane Katrina (where he also got into trouble for having appointed cronies to important jobs), Mr Bush's approval ratings have fallen to around 40%. Americans by a wide margin now claim they will vote for congressional candidates who oppose him. His main domestic goal—reforming the Social Security pension system—looks beyond reach already.

As for foreign policy, support for the American-led invasion of Iraq has fallen sharply this year. This week a rare triumph—the passing of the new constitution—was balanced by the 2,000th American death in the conflict. As for scandal, the Republican leader in the Senate, Bill Frist, is under investigation for insider dealing and the House leader, Tom DeLay, has been indicted on charges to do with campaign fraud.

It would be foolish to count Mr Bush out—especially if Mr Rove survives. The Republicans still look well placed to hang on to Congress next year—if only because the Democrats are so shambolic. The withdrawal of Ms Miers may even come to be seen a turning point. But only if Mr Bush learns from his mistakes.

The main priority is to clean up the White House and to remove the tinge of cronyism. After all, whenever Mr Bush appoints well qualified people, he gains. He won plaudits for appointing John Roberts to be chief justice of the Supreme Court; the same broadly applies to making Ben Bernanke head of the Federal Reserve. When he appoints people like Ms Miers or Michael Brown, the erstwhile horse-expert whom he put in charge of the Federal Emergency Management Agency, it returns to haunt him.

Choosing somebody who is intellectually first-rate for the Supreme Court would be a good first step. But the broom must surely sweep more briskly than that. Whatever comes of Mr Fitzgerald's investigation, it is an excuse for a clean-out of some of the more established retainers, who have underperformed. It is well past time for Mr Bush to call Donald Rumsfeld to account for the disasters in Iraq and much more.

Mr Bush should take the same approach to Congress. One reason why spending is out of control is the worrying links between the Republican Party and lobbyists. Far too much money has been spent on boondoggle projects of one sort or another. Mr Bush, who has yet to use the presidential veto even when presented with absurdities like a bridge to nowhere in Alaska, should not tolerate

any more follies.

Mr Bush is an odd mixture. Few recent presidents have come to the White House with such a bold vision to change society or been so willing to spend political capital in that quest. But his boldness will come to naught if it is not followed up by efficient execution. Unless he tidies up his administration after this storm, Mr Bush runs the risk of sullying the ideas that he has championed.

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India and China

What's to stop India and China?

Oct 27th 2005
From The Economist print edition

India and China could grow even faster but for their political timidity

FOR the past two years and, according to projections, this year and next as well, the Indian economy has managed to grow at around 7% or better. That allows optimistic souls, in London, New York and Tokyo as well as in Delhi and Bangalore, to hope that India might now be on the verge of repeating China's awesome transformation. By averaging annual growth of 9.5% for almost three decades, China has lifted hundreds of millions out of poverty in the most rapid and far-reaching economic transformation in history.

Such talk, alas, is just that: optimistic. Even India's prime minister, the courteous and intellectual Manmohan Singh, admits as much. He admires China's discipline in driving through big infrastructure projects and economic reforms, he says; but notes (with diplomatic phrasing), that China is “more focused than India, as a democracy, can afford to be.” It is, he reckons, a price worth paying; he has no desire to see India change its political system.

Yet just at the moment, democracy is proving far from helpful to Mr Singh as he struggles to move India's economic reforms on to the next stage. In the early 1990s, then serving as finance minister, he became every economist's darling by introducing measures that set India back on the path to growth. Tariffs were slashed, exchange controls scrapped, the “licence raj” that strangled business in red tape largely abolished. In retrospect, that was the easy bit.

The reforms of the 1990s required vision, but tended to benefit everyone and harm no one. What India needs now is a raft of supply-side reforms that will, in the short term at least, hurt powerful interests. These are principally the trade unions which, through their control of the Communist parties that in turn prop up Mr Singh's minority government, are able to hold him to ransom. As we report (see article), the Communists have more or less brought Mr Singh's reforms to a halt. He has been unable to continue the task of privatising the plethora of inefficient state-owned businesses. He has found it almost impossible to ease the system of caps that limit foreign direct

investment in many big sectors, notably retailing. And labour market reform is not even being discussed.

It is not fair to blame Mr Singh for all of this, though he might have tried harder. He is in office but not in power. Although he is prime minister, it is Sonia Gandhi, the president of the Congress party, who takes the big decisions. Under her rule, the party has reverted to its traditional stance; left-leaning and not very interested in reform. For its part, the opposition Bharatiya Janata Party (BJP), which was once truly reformist, has lapsed into internecine and perhaps terminal bickering about the virtues of Hindu fundamentalism.

The gloom should not be overstated: India today has a dynamism that has never been there before: witness the incredible growth of outsourcing companies, now doing legal and medical work for clients around the world, not just running their call-centres. The momentum from the earlier reforms continues, and despite his difficulties Mr Singh has been able to introduce a national rate of value-added tax, and pioneering public-private partnerships for road building. It probably is the case that the earlier reforms focused too much on the affluent city-dwellers at the expense of the rural poor—who voted the BJP out of office last year—so a period of consolidation may be no bad thing. Sooner or later, though, India will have to tackle its remaining rigidities. The fate of Mr Singh, increasingly these days seen as someone to be pitied rather than admired, is a reminder of just how powerfully politics can constrain economics.

So too in China

That is so in India, perhaps, but surely not in China, which may lack the benefits of democracy, but is at least free of its pitfalls? Only up to a point. China is clearly not a democracy in the sense of having an elected leadership or multiple political parties, but that is not the same thing as saying that its people have no power. The really interesting thing about the presidency of Hu Jintao, who completed the drawn-out business of assuming power only a year ago, is just how nervous he appears to be about popular discontent, and the lengths to which he is going to appease it.

China officially saw no fewer than 74,000 riots and demonstrations last year—some small and peaceful, but many large and a number even violent. Just like Mr Singh in India, Mr Hu is consequently being forced to concentrate much harder on the rural poor than on the coastal cities. Cleaning up corrupt and abusive government is one priority for him, reducing the burden of tax on the countryside another. Tackling pollution, which invariably hurts the poor more than the affluent, has become a third.

As in India, this renewed concern about discontent among those left behind by progress is tempering liberalisation. This is most obvious in the area of the Chinese economy which needs it most: the banking sector. As we report (see article), the Chinese government clearly recognises that its banks are under-capitalised and insufficiently profitable, and it has taken some impressive steps to correct these problems with determined efforts to recapitalise the weak and clear up at least part of what used to be a mountain of bad debt.

But it has not been anything like brave enough. The government has not addressed the root cause: the big banks remain, ultimately, under the control of the government and not the rules of commerce, which is why foreign investment—which would improve efficiency by opening banking to lots more competition—remains restricted, just as it is in India. As long as this is so, the pressure to allocate credit on the basis of political patronage rather than market efficiency will persist. Fearful of ceding too many levers of control to the private sector, let alone foreigners, China's nervous leaders are still shying away from the toughest decisions. The method of getting rid of a government that is seen to be failing its masses might be different—revolution in China,

the ballot box in India. But the world's largest autocracy and its largest democracy have more in common than one might think.

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Syria

Converting Damascus

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AP

A suitable case for behaviour modification, not regime change

Get article background

SHORTLY after America toppled Saddam Hussein in 2003, in the brief interval when it looked as if installing a democracy in his place might be plain sailing, some members of the Bush administration pondered whether it might be a neat idea to knock over the other Baathist dictator, Syria's President Bashar Assad, as well. It is a good thing wiser counsel prevailed. Enough violence is bubbling in Iraq without throwing a second collapsed Arab state into the pot. But what if Mr Assad should start to collapse of his own accord?

A remarkably inept dictator

Whether Mr Assad is in fact on the brink of losing power is hard to say. Like Iraq's internal workings under Mr Hussein, Syria's under Mr Assad are pretty much a black box. For all any outsider can tell, Mr Assad may be able to hold on to his job for a good while longer. But since inheriting the Syria franchise from his father Hafez in 2000, the son has turned out to be a remarkably inept dictator. He has antagonised the United States by letting jihadists and other insurgents enter Iraq from his territory. And he has made an astonishing sequence of mistakes in Lebanon, which his father spent quarter of a century turning into a vassal state. At the beginning of this year, Syria was still Lebanon's master. Now its army has been forced to leave, and Syria stands accused in the United Nations Security Council of having organised or connived in the murder of Lebanon's former prime minister, the well-liked Rafik Hariri, along with 22 others, on the Beirut seafront last February.

Although nobody has yet been tried or convicted for this murder, Detlev Mehlis, the diligent

German prosecutor appointed by the Security Council to undertake an independent investigation, reported this week that many leads point directly towards Syria's top security officials (see article). And Syria certainly had a motive. At a time when both France and America were pressing it to leave Lebanon, Mr Hariri refused to take the Syrian side. According to some witnesses, at a meeting in August 2004 Mr Assad threatened Mr Hariri with violence if he persisted in his obstructive ways. A month later, Mr Hariri said he would resign but made it plain that he would fight on from opposition. He was assassinated on February 14th 2005 by a sophisticated bomb attack on his convoy.

So what should now happen? The first demand of the Lebanese is that justice should be done. And though this will be difficult, there is a half-successful precedent.

Four years ago, a Scottish court sitting in the Netherlands convicted a Libyan intelligence agent of planting the bomb that destroyed an American airliner over the Scottish town of Lockerbie in 1988 and killed 270 people. Libya's Muammar Qaddafi was persuaded to hand over the two suspects (one was acquitted) after the Security Council imposed sanctions. Mr Qaddafi insisted on his innocence but paid compensation to the victims' relatives. Whether he gave the order himself was never resolved. He was left in peace—though out in the cold—until buying a sort of respectability by admitting to and dismantling a secret nuclear-bomb programme in 2003.

To many of the Lockerbie victims' relatives, the jailing of an underling seemed scant justice in what always looked like a mass murder ordered from the top. In Lebanon, likewise, many people will feel let down if senior members of the Syrian regime identified by Mr Mehlis are allowed to escape justice. Whoever is brought to trial, the suspicion is bound to linger that the murder required the approval of Mr Assad himself. And even if he were willing to hand over his brother and brother-in-law, both of them implicated though not yet named as suspects, he is hardly likely to submit himself for trial. So if Mr Assad himself gave the order, perfect justice cannot be done while he remains in command of Syria.

Given that even a not very good dictator is a bad thing, should America and France, which took the lead in squeezing Syria's army out of Lebanon, now engineer the downfall of the regime itself? That would be a gamble. Mr Assad has purged his country of an effective opposition. It is therefore impossible to know who might take his place if he fell. A clone might emerge from his inner circle, or Syria could be convulsed by a Sunni revolt against the Assads' minority Alawite clan. In neither case would the Syrian people or their neighbours necessarily benefit. Syria, after all, is not the republic of fear Iraq was under Mr Hussein. Unlike his father (who had some 20,000 people, mostly civilians, slaughtered in the city of Hama in 1982), the younger Mr Assad has not been a mass-murderer, even if he orders the occasional assassination.

Better to use Mr Assad's present weakness as an opportunity to change Syria's behaviour, not its regime. In particular, Syria should be made to stop interfering in Lebanon, which its proxies continue to intimidate even though its army has withdrawn; end its support for the Iraqi insurgency; and close the offices of the Palestinian rejectionist organisations that use Damascus as a base from which to organise attacks on Israel and undermine the Palestinian Authority of Mahmoud Abbas.

Bring on the Russians

In the Security Council this week, the Russians gave a frosty response to a draft resolution from America, France and Britain that would empower Mr Mehlis to complete his investigation and pave the way for sanctions if Syria refuses to co-operate. The Arab League also said it opposed sanctions—for now. But this may not, and should not, be the last word.

Although Syria was a Soviet protégé, and has friends in its foreign ministry, Russia's president, Vladimir Putin, may come to see the folly of protecting a dictator who repels the many Arabs who are tired of their leaders behaving like mafia bosses. To bring Mr Putin on board, however, America would be well advised to pipe down and let France, whose president was a friend of Mr Hariri's, make the running in the Security Council. If the Syrian regime collapses of its own accord, or at the hand of its own people, so be it. But the world has no appetite for more American-led regime change. Loose talk about that will do more to help than to hurt the deservedly friendless Mr Assad.

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The Federal Reserve

Big Ben strikes gold

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AP

The new boss of America's Federal Reserve will need a lot of luck

ECONOMIC commentators were almost unanimous this week in applauding President Bush's decision to nominate Ben Bernanke to replace Alan Greenspan as the next chairman of the Federal Reserve. This partly reflected relief that Mr Bush had not chosen another of his political cronies for a top post, this time America's most important economic policymaking job. But Mr Bernanke also has impressive credentials: he is one of the world's best monetary economists, and served as a Fed governor from 2002 until this June, when he became chairman of the President's Council of Economic Advisers (see article). Of the outside candidates, he was the strongest.

He was not, however, *The Economist*'s first choice. Our doubts about Mr Bernanke still stand: he has been an academic economist for most of his career and has relatively little experience of financial markets. He will need to learn fast.

Unlike some critics, we are worried not that he will go soft on inflation, but about other elements of "Bernankenomics". In 1999 Mr Bernanke co-authored one of the first academic papers arguing that central banks should not worry about rising asset prices unless they affect inflation. He thus provided intellectual ammunition for the Fed's inaction during the late 1990s stockmarket bubble and the current housing bubble. But we, along with officials at the Bank of England, the European Central Bank and the Reserve Bank of Australia, reckon that he is wrong. Central banks should sometimes raise interest rates to curb asset-price booms.

Another of Mr Bernanke's big ideas is that a global saving glut is to blame for America's current-account deficit, not domestic profligacy. However, Mr Greenspan himself has argued that surging house prices and massive home-equity extraction explain the fall in America's household saving in recent years, and hence much of the increase in the current-account deficit. In other words, a good part of the deficit is made at home not abroad. At some point there will be a correction, involving a weaker dollar and possibly higher bond yields.

A change of Fed chairman is always a nail-biting time for financial markets. If confirmed, Mr Bernanke will take charge of the Fed at a particularly tricky time, when the American economy looks unusually unbalanced, with a record high current-account deficit, the biggest housing bubble in history and rising inflation. Awkwardly, his need to establish his anti-inflation credibility may leave him little room to cut interest rates to cushion the economy when the housing bubble deflates. If financial markets then get the jitters, Mr Bernanke's dazzling academic credentials will count for little.

Mr Bernanke's toughest test will be to accept unpopularity if the economy turns sour. Mr Greenspan has been one of the most popular central bankers of all time. But central bankers are not supposed to be like rock stars, and Mr Greenspan's god-like image has caused firms, households and investors to be overly confident about his ability to keep the economy growing. It would be good for the Fed to be less dominated by its chairman. As Mervyn King, the governor of the Bank of England, has argued “successful central bankers should be seen neither as heroes nor villains, but simply as competent referees, allowing the game to flow.” As a big ideas man rather than a policymaker, Mr Bernanke may not be boring enough to be a good Fed chairman. Whatever happens, given the tricky times ahead, he will need to develop a thick skin: he will be blamed when things go wrong, even if it is not his fault.

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Economist.com OPINION

Kashmir's earthquake

A humanitarian failure

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AP

For so many it is already too late; but much more can be done to help the people of Kashmir

Get article background

THE global broadcasters have packed up their satellite dishes and moved on. On television screens, images of hurricane winds battering Florida have supplanted the scenes of infants buried in Kashmir's rubble. But the earthquake that shook both Pakistani and Indian parts of the disputed territory on October 8th continues to wreck and end lives by the thousand. With barely two weeks until the winter snows might begin, relief workers have still not reached many remote hillside villages on the Pakistani side. More than 54,000 people are known to have died, and an estimated 3.3m have lost their homes. A second disaster looms, of mass death from cold, hunger and disease. This second disaster is probably inevitable, such is the logistical nightmare of relief work in the inaccessible parts of this rugged Himalayan region (see article). But the catastrophe could still be mitigated.

Two weeks after the United Nations launched an emergency appeal for aid to cope with the disaster, less than a sixth of the $550m it needed at once had been raised. At the same stage, an appeal launched after last December's tsunami had plenty of funds. It is hard to know why the world has taken so long to reach for its wallet. Perhaps the tsunami, killing hundreds of thousands, deadened compassion. Perhaps it was that Kashmir has dropped off rich-world tourist itineraries, unlike the beaches of Thailand and Sri Lanka.

Whatever the reason, the earthquake has not provoked the response from the rest of the world that it needed, despite the best efforts of the UN. A donors' conference in Geneva on October 26th mustered fresh pledges of $580m. But that covered reconstruction as well as emergency relief. Too little, too late. The United States, in particular, so quick to call on Pakistani support after the

attacks of September 11th 2001, has largely squandered an opportunity to win goodwill. Although it has provided aid, including in the most useful of forms—the loan of helicopters—many Pakistanis feel it could have done much more, much sooner.

Politics as usual

They level the same criticism at their own government. Some is unfair: whatever it had done, it would not have been enough, so great was the calamity. It also seems the wrong moment for apportioning blame, as soldiers and helicopter pilots are performing heroic feats to rescue those still cut off. Moreover, the government of Pervez Musharraf did some things right, not least in its immediate embrace of most of the foreign help that was on offer. This showed a humility that was echoed when General Musharraf later admitted that the army's initial response had been slow. It also involved political risk—in accepting aid from India and Israel, for example, and in allowing the deployment of American and NATO soldiers in the affected regions.

The effect of the earthquake, however, was an indictment of the lack of preparation. One reason so many died is that shoddily constructed public buildings—schools and hospitals—collapsed easily. And the army cannot escape blame for the shortcomings in the relief effort. General Musharraf centralised relief work under two of his generals, showing a lack of faith in the civilian administration that bodes ill for his professed plans to restore full democracy.

That politics and a military turn of mind still triumph over humanitarian concerns is also sadly evident in Pakistan's response to India's offers of help. It rejected helicopters because they would come with Indian soldiers, but offered to open the “line of control” dividing Kashmir to allow family reunions and ease relief work. Three weeks after the disaster, the two countries are still haggling about the “modalities”, apparently more interested in scoring political points than saving lives. Grotesquely, a Pakistani minister said he would lead a convoy of relief lorries into Indian Kashmir. Did he imagine that the hungry and unhoused on the Pakistani side would cheer him on his way?

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Economist.com OPINION

Product placement

Ride and prejudice

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Why the return of product placement is nothing to worry about

IT IS a truth universally acknowledged, that a single man in possession of a good fortune, must be in want of a Jaguar XK 4.2-S. So might “Pride and Prejudice” have started had Jane Austen, who was paid £110 (£3,200, or $5,700, in today's money) for one of the bestselling novels ever, been lucky enough to live in an era which offered the mutually beneficial partnership between creative talent and commercial sponsorship known as product placement.

See how swiftly the hero runs in his flash new trainers? Notice how luxuriantly the shower gel foams on the heroine's loins? That's probably because the companies that make those products have paid the producers of those programmes fat fees to portray their wares nicely. Product placement, which gave birth to the original soap operas created to sell washing powders, is back (see article).

Digital technology is the reason. Viewers can now effortlessly skip the ads, so broadcasters and the companies that used to buy airtime for commercials are trying to find better ways to catch people's attention. Product placement is one promising option, but it is controversial. It is allowed in America but mostly banned in the European Union. European producers and broadcasters complain that this is unfair because their American rivals benefit from a source of income denied to them, and senseless because American programmes anyway appear on European screens. Some European producers have been breaking the rules. Germany's public broadcaster, for instance, has been accused of taking money from a group promoting Turkish membership of the EU. That must have been tough to write into the script (Maria: No, no, our love can never be! Klaus: Yes, yes, my heart! We are destined to be together, as surely as Turkey is bound to be one with the EU).

The EU is therefore planning to legalise product placement, but the proposal faces some opposition. Viewers watching ads, say the critics, are fair game because they know they're being

sold stuff. When they're watching programmes, by contrast, they don't realise that products are being promoted. As they see the hero ply the compliant heroine with some seductive libation, sillier viewers may really believe that's the way to get sultry blondes into the sack; and the idea may seep subliminally into the brains even of the more discerning, who may, to their surprise, find themselves filling their trolleys with sickly liqueur next time they're in the supermarket.

But if advertising that slips imperceptibly into people's brains were to be banned, a great deal of what goes on now would be outlawed. After all, drivers spinning past hoardings don't necessarily consciously clock the message they've seen; often they file it unconsciously—as you, browsing through these pages, may well absorb the notion that an expensive watch or a new phone will change your life in some vague but enticing way. As for people who believe the literal truth of what they see in soap operas—well, no amount of regulation can protect them from themselves.

Anyhow, governments don't need to police entertainment. Content-producers will do it themselves. When Fay Weldon, a novelist, wrote a book for Bulgari, a jewellery manufacturer, a few years ago, it was not widely viewed as a literary gem. Neither she, nor anybody else with a reputation worth keeping, has tried that again. Which is just as well: the world would have been a poorer place had Mr Bingley been more interested in his ride than in the Bennet girls.

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Economist.com OPINION LETTERS

On abortion, Darfur, humanitarian aid, Kashmir's earthquake, Russian superstition, Iraq's constitution

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Catholic choice

SIR – It is important to note that Colombia's Catholics, who comprise 90% of the population, support the liberalisation of its abortion laws ("Last bastions", October 8th). A poll, conducted by Católicas por el Derecho a Decidir (Catholics for the Right to Decide), in September 2003 demonstrated that the vast majority of Colombians support access to legal abortion when the woman's life is in danger, her health is at risk, the fetus has severe abnormalities or the pregnancy is the result of rape. The Catholic tradition is based on respect for the conscience of each individual person. Church law recognises the right of Catholics to follow their conscience, even when their decision disagrees with a teaching of the church. The record of respect for human rights demonstrated by the Constitutional Court of Colombia is legendary in the region and in the international human-rights community. We are certain that it will respond to Monica Roa's legal challenge to overturn the ban on abortion with the judicial independence and interests of Colombia's women that have marked so many of its historic decisions.

Frances Kissling
Catholics for a Free Choice
Washington, DC

SIR – George Bush's administration and its fundamentalist minions have imposed its anti-abortion agenda abroad, which is having a chilling effect. The "Global Gag Rule" stops the United States providing assistance to reproductive-health services that include abortion in any way. Aid recipients have been helpless in advising women about legal alternatives to unsafe abortion and barred from openly joining the movement for decriminalisation. The policies of the Bush administration have therefore impeded progress towards the safe, legal termination of unwanted pregnancies, which has contributed to illnesses and deaths resulting from botched clandestine abortions. Should anti-choice forces in the United States succeed in repealing the constitutional right to abortion, the ramifications for reproductive rights throughout the western hemisphere will be devastating.

Carmen Barroso
International Planned Parenthood Federation
New York

Arab indifference

SIR – Since the Sudanese government and its *janjaweed* proxies began their war against Darfur's civilians almost three years ago, other Arab governments have done nothing to stop it and little to succour its mostly Muslim victims ("Darfur's despair", October 15th). Western and Arab media

have also been curiously silent on this matter. Apparently it is worth pondering earnestly how Arab nations can be dissuaded from supporting terrorism and encouraged to embrace democracy, but Arab indifference (or worse) to mass murder and gang rape is just one of those things we have to accept.

Joseph Britt
Kennesaw, Georgia

Aid reform

SIR – The current food crisis in southern Africa was predicted months ago, yet the UN World Food Programme's appeal for the crisis is still short of over $150m ("From hand to mouth", October 8th). In Niger, it was the same story. As the food crisis in the west African country hit its peak in July, UN appeals for the crisis were still underfunded by half. People died as a direct result of this delay in donor funding. The current system, in which rich countries wait until a crisis hits the headlines before providing enough aid, urgently needs reform. Next month, the UN General Assembly has an opportunity to make this desperately needed change. It must agree to reform the UN's central emergency fund so that money is available as soon as countries such as Niger and Malawi need help. UN member states must also promise to pledge $1 billion into that fund on top of their existing humanitarian aid budgets. This would be 2% of the extra aid money pledged at the G8's meeting in Gleneagles in July.

This reform would save money. The UN has estimated that it is 80 times more expensive to save an acutely malnourished child than to prevent that child from becoming malnourished in the first place. And it would save lives, making preventable crises a thing of the past.

Phil Bloomer
Director of campaigns and policy, Oxfam
Oxford

Disastrous response

SIR – An opportunity to open the line of control between Pakistani- and Indian-administered Kashmir has indeed been missed ("A double tragedy", October 15th). However, criticism of the Pakistani and Indian armed forces in their response efforts is overdone. Parts of both forces stationed in Kashmir were knocked out, their equipment lost and their ability to respond quickly destroyed. Blocked roads and bridges, lack of rail and small upcountry airfields, coupled with rain and snow, made swift access impossible except by helicopter.

Criticism is cheap and panders to the distraught, whereas relief is, in part, achieved by peace of mind. Lambasting the best efforts of Pakistan, India and the world will only exacerbate this problem.

George L. Singleton
Hoover, Alabama

SIR – The Pakistani and Indian earthquake victims' disappointment in government's slow response to their needs is part of a larger pattern. From America and Hurricane Katrina, to Japan and the Kobe earthquake, via Indonesia and the tsunami, the story always seems to be the same. People who believe that governments can act as saviours during times of crisis are mistaken. Individual preparedness, and the realisation that large scale efforts take time to execute, must be the order of the day. While governments can and should do much more to prepare a response to emergencies, so should individuals.

Joe Zimmerman
Boise, Idaho

Russian resurrection

SIR – According to Russian folklore, great men never die; they simply go into the ground and sleep for a while, to return at some later date when their country needs them ("Bury Lenin", October 8th). Most Russians feel this way, and a thousand years of Christianity hasn't done much to convert them, just as 70 years of communism hasn't made atheists of them.

Russian superstition also has it that the corpses of great men do not deteriorate after burial. This is why Lenin is kept on display and why the corpses of Nicholas II and his family were destroyed; the Russians fear a dead body as much as they do a living man.

David A. Roach
Corpus Christi, Texas

Constitutional question

SIR – How interesting that a newspaper such as yours should find itself advocating the Iraqi constitution when a few months ago you opposed the European one ("Ballots amid bullets", October 15th). Perhaps an official role for religion and a requirement that European Court of Justice judges be educated in the law of Leviticus would soothe your opposition to the latter document?

Kyrre Holm
Oslo, Norway

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Reform in India

Democracy's drawbacks

Oct 27th 2005 | DELHI AND KOLKATA
From The Economist print edition

AP

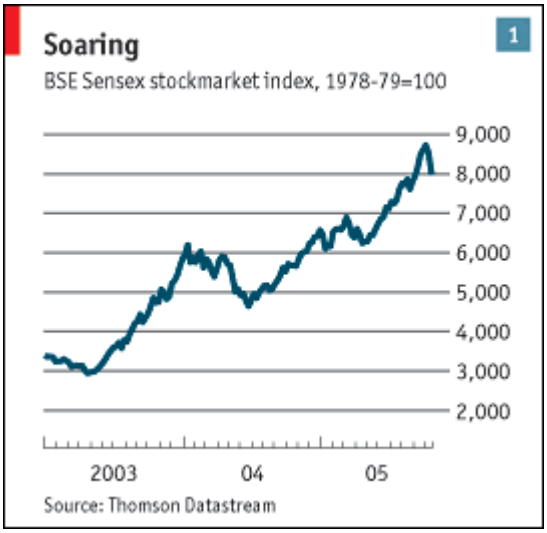
Sustained growth in India would be all the more impressive if the government could pass its reforms. But the road is blocked by politics

Get article background

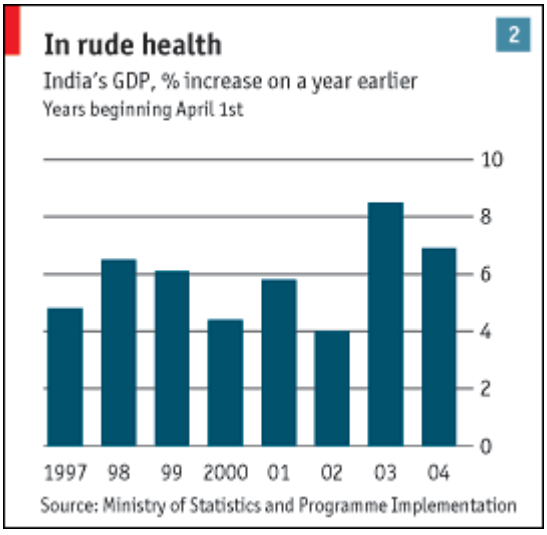
IN CITY after city, India is booming. Visit Delhi or Mumbai or Hyderabad, and they are full of shining new office towers and American-educated MBAs. The suburb of Palm Meadows (pictured) outside Bangalore, the home of high-tech and outsourcing, looks like the richer blocks of Los Angeles. The stockmarket has risen by more than 20% this year (see chart 1), though it slipped back a bit this month. In the second quarter, India's GDP grew by 8.1% compared with the same period last year. After annual growth of around 7% in 2003 and 2004 (see chart 2), the country is on course, many economists think, to repeat the trick this year and next.

India's IT companies are world-beaters. Firms such as Tata Consultancy Services, Infosys and Wipro, which owe their success to large, co-operative software-development projects for companies in America, are now beginning to compete directly with the big IT multinationals for large consultancy contracts. Out of this IT infrastructure has grown a huge business in "outsourcing" almost any business process that can be performed remotely, from answering a call in a help centre to interpreting an X-ray. The largest outsourcing firm relaunched itself in September as Genpact, partially disguising its origins as the Indian back-office of General

Electric, and expects to exceed $1 billion in annual sales by 2008.



These service businesses have thrived because they have capitalised on India's strengths—computer skills, fluency in English—and are not hostage to its weaknesses. Yet those weaknesses are all too obvious, and are the reason why India on many counts still lags behind its neighbour-rival, China. India has lousy infrastructure, bumbling and burdensome regulation and restrictive labour laws. And economic reform now appears to have stalled in political recriminations.



Last year's election gave no party a clear majority. A delicate arrangement allowed Manmohan Singh, of the left-of-centre Congress party, to take office as prime minister, while a committee was set up to negotiate policy between Congress and its coalition partners (together called the United Progressive Alliance or UPA) on the one side, and the Left Front of Communists and other left-wing parties on the other. The committee, however, has not managed to meet since June, though on October 26th there were rumours that it was about to. Meanwhile, the Communists—without whom the coalition has no majority in Parliament—are getting truculent. They staged a four-month boycott of the co-ordination committee to press their policies and then, in concert with the trade unions, called a one-day general strike on September 29th. It was ignored in many places, but the banks, along with the Communist stronghold of Kolkata (Calcutta), were paralysed.

When Mr Singh was finance minister, in the 1990s, it was he who pushed through the measures that kick-started reform in India. Without the support of the Left Front, however, he can do nothing more. His most significant legislative achievement to date has been a law that guarantees 100 days' employment to every household in India's 200 poorest districts. Though the Left Front loves it, many economists reckon that much of the money—as much as 1% of GDP, by some estimates—will be wasted or stolen.

The list of what Mr Singh has been prevented from doing is much longer. Completely ruled out has been any progress on liberalising India's notoriously rigid labour laws. The key battleground is a rule preventing any company with more than 100 employees from making redundancies without obtaining approval from local labour boards. According to the Left Front, this protects workers from unscrupulous employers. In fact, it makes employers wary of taking on new staff, opening new factories or, in the case of smaller companies, growing beyond the threshold of 100. It protects unionised labour, in short, at the expense of those not in work.

The Left Front, which draws most of its support from organised labour, does not greatly care. Its eyes are on state elections due next year in West Bengal (whose capital is Kolkata) and Kerala, the two biggest states where the Communists are strong. Those who are losing out from unreformed labour laws are hundreds of millions of people now marginally employed in the countryside. These people need jobs in manufacturing if India is to improve its record on poverty, as well as growth. Jobs could be found in the labour-hungry textile industry, especially now that, with the ending of the developed world's protectionist Multi-Fibre Arrangement, India's textile exports are booming. As it is, a jobless boom is going on in manufacturing, which is growing at 7% annually, but without increasing employment.

Touches of xenophobia

India's antiquated laws are not only preventing it from exploiting the textile boom as successfully as China (whose textile businesses are so successful that they provoke retaliation). They are also pushing it far behind China in terms of foreign direct investment. FDI has been the most important driver of China's growth, not just because of the money involved (more than $60 billion last year) but also because of the technology, expertise, marketing relationships and much else that this money represents. India's showing has been far less impressive: about an eleventh of China's haul last year (see chart 3).

One chief reason for the discrepancy is that India imposes caps on FDI in a host of economically important, or politically sensitive, sectors: insurance, aviation, coal-mining, media and much else. Chief among these is retailing. Though franchise operations are allowed, foreign direct ownership is banned, which explains why even Delhi's smartest shopping areas are scruffy and chaotic places with limited stock.

Mr Singh's government would like to raise the caps, and had some success at first. It proposed in February, for example, that the cap for telecoms investment should be lifted from 49% to 74%, and this has just, at last, been approved. But the Left Front is violently opposed to any tinkering with the rules for FDI in retailing. Its leaders appear to accept that the advent of, say, Wal-Mart would generate many jobs, since much of what the company sold would be domestically produced (Wal-Mart spends $15 billion a year in China). But they worry that millions of small retailers would be put out of work. For those who want to move out of farm work, a small shop is often their first choice.

Mr Singh remains optimistic, but on slender grounds. With the Left Front so adamant, nothing is likely to happen. And the same is true of privatisation, or its younger sibling, disinvestment, the selling of minority stakes in state-controlled companies. From the very start of its tenure, the government was forced by the Left Front to agree not to privatise nine so-called “crown jewels”, or leading state-owned companies. But the Left has taken advantage of its position to go beyond what was originally agreed. When, in June, the government announced plans to sell a 10% stake in Bharat Heavy Electricals, an engineering firm, the Left Front vigorously objected. Although the sale does not require legislation, and so could be enacted by the minority government, the government shows no stomach for doing so.

Another disappointment—though the word is perhaps inappropriate, since no one ever expected a

Congress government to have the necessary courage—is the failure even to attempt to do anything about the mountain of subsidies that distort the Indian economy. Often badly targeted, benefiting middle-class people more than the poorest, they consume a shocking 14-15% of GDP.

Worst of all, Indian politics may actually be retreating to its bureaucratic past. Take oil pricing, a complex statist rigmarole that had been moving from the hands of government to those of a regulator. Under Mr Singh, price decisions are again being taken by the government.

The prime minister's instincts are sometimes depressingly bureaucratic. Faced with obvious and longstanding problems, he commissions a study on them. The latest strategy document appeared in September from a specially convened National Manufacturing Competitiveness Council. It listed the most pernicious difficulties for manufacturers: power shortages, taxes and the “inspector raj”. No one was surprised by these, or felt much hope they would be fixed.

Removing the brake

It may seem odd, if reform is so important, that the economy is doing so well without it. There are a number of reasons. The biggest is that the Indian economy is so strong, structurally and cyclically, that it can ride out a period of wobbly policy. India's young population gives it a fast-growing workforce and a declining proportion of dependants. Over the next few decades, that will be good for savings and investment. Industry, meanwhile, has recovered from a splurge of over-investment in the mid-1990s. It has improved efficiency and is now both reaping the benefits and investing again in new capacity.

The government started to get out of business's way in the 1980s and, especially, after a balance-of-payments crisis in 1991. At that point Mr Singh, as finance minister, was given the freedom to bring in reforms by an unexpectedly brave prime minister, Narasimha Rao. Since then, government has been unable to put an absolute crimp on growth. Many important reforms—especially trade liberalisation, but also the dismantling of the “licence raj” of bureaucratic obstacles to enterprise—are well in train and not in reverse.

Reuters

Too many are still losing out

Almost every budget since 1991, including this year's, has cut import tariffs and freed more industries from “reservation” for small firms, a big hindrance to competitiveness in businesses that might benefit from economies of scale. This year, moreover, saw the introduction of one long-planned reform, a standardised value-added tax imposed at state level. Typically, politics meant that not all states fell into line, and implementation has been patchy. Yet the tax may eventually

not only bring new fiscal stability, but also reduce the burden of cascading excise and sales taxes that is one of the biggest handicaps facing manufacturers. Modest, piecemeal reform, in other words, is not quite dead.

The government's priorities—investment in infrastructure, agriculture, basic education and primary health care—are also right, given that the big macroeconomic stuff was mostly done in the 1990s. But they all need money, and that requires fixing the budget. India's fiscal deficit is now 8% or so of GDP if both state and central governments are counted—an improvement after six years of double-digit deficits, but still too high. Public finances have been in a mess for so long that it seems almost impolite in government circles to mention them.

The deficit, which goes largely on interest payments (40% of recurrent spending), defence, subsidies and civil-service wages and pensions, leaves little room for big capital investments. Some new airports, ports and roads are being built, and the “Golden Quadrilateral” highway, linking India's four biggest cities, is being expanded to six lanes. But Mr Singh wants a good deal more. Improving India's infrastructure, he says, is his top priority. Hence his government's zeal for “public-private partnerships” to finance and construct it.

A standard concession agreement is to be produced soon, modelled on successes with toll roads, where concessionaires have put in competitive bids for government grants. For some projects, the government does not need parliamentary approval and can proceed anyway. Other projects, however, such as airports, will run into objections from the left. It is therefore hard to see these partnerships making much of a dent in what Montek Singh Ahluwalia, the prime minister's chief planner, calls India's “infrastructure deficit”.

Might the left-wing parties ever become less obstreperous, and realise that reforms like these are of benefit to all Indians? It is possible. Jairam Ramesh, a Congress member of parliament who played a big role in writing the “common minimum programme” that defines relations between the UPA and the Left Front, floats the interesting theory that, now that Congress has enacted the Employment Guarantee Act that the Left was so keen on, the Left may prove a little keener on asset sales. They would, after all, be a way of paying for all those jobs.

From the Left Front come faint signs of accommodation. Prakash Karat, the general secretary of the CPI (M), the most important party within the group, is, like Mr Ramesh, adamant that full-scale privatisation of profitable public enterprises is not on the agenda. But he says the party is “ready for a discussion” on how to raise resources for spending on the poor.

Among the most eloquent advocates of a re-think is, in fact, a senior Communist, Buddhadeb Bhattacharjee, chief minister of West Bengal, a state of 82m people run for 28 years by the Communists and their allies. On September 30th, the day after Communist-affiliated trade unions had brought his capital, Kolkata to a halt, he could scarcely conceal his exasperation. He told *The Economist* that the trade unions—and many of his party comrades—had become “one-dimensional”, representing only the interests of the 30m or so workers in India's “organised” sector.

Mr Bhattarcharjee concedes that some of his colleagues in Delhi do not seem to grasp that economic reform could benefit a much bigger number of workers than those who belong to unions. If they do, they perhaps see political benefits in ignoring it. But “Here, we are running a government. We have to fulfil the aspirations of the people.” To that end, he is trying to turn Kolkata into a hub for the information-technology industry by declaring it a “public utility” where strikes are banned, and has started going abroad to bang the drum for inward investment.

Jobs for the poor

Such enthusiasm may start to shift the political balance back towards reform, but it looks unlikely. For the foreseeable future, both left-wing intransigence and lack of decent infrastructure—in particular, a chronic shortage of electricity—will constrain India's growth. An average annual rate of 6-7%, as in the past decade, does not seem a tall order. But a gear-shift to a durable growth rate of 8-10% still seems out of reach.

Without it, that burgeoning workforce may seem less of an advantage. Shankar Acharya, a former government economist now at a Delhi think-tank, worries that between now and 2051 nearly 60% of India's population increase will come from four “populous, poor, slow-growing northern states with weak infrastructure, education systems and governance”.

China has sucked surplus agricultural labour into factories by the tens of millions. India's manufacturing industries, by contrast, have progressed by becoming more productive. They are still not a big source of rural employment. As a good liberal economist, Mr Singh says he does not believe in having an “industrial policy” or picking favourites. Create decent infrastructure, and industry will come—and he sees huge potential, as do many others, in food-processing. His finance minister has spoken of 12m new jobs in the textile sector alone in the next five years.

They are sorely needed. India's information-technology firms are world-beaters, but the entire IT and office-service industry employs only about 1m people. None of the Asian tigers, not even Singapore, managed its rapid climb into the ranks of middle-income and rich countries without a boom in export-oriented manufacturing. India is unlikely to be different.

When he speaks of following the “Chinese model”, Mr Singh seems to admit this. But it remains sadly true that the free market that has helped the tigers so much often works better in Communist China than in India—not least thanks to India's own democratically elected Communist politicians.

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The White House

Under siege

Oct 27th 2005 | WASHINGTON, DC
From The Economist print edition

Getty Images

George Bush's problems go much deeper than just a zealous special prosecutor

Get article background

WHEN *The Economist* went to press, it was not clear who, if anyone, was to be indicted by Patrick Fitzgerald, the special prosecutor in “Plamegate”. But since those being probed included Dick Cheney, his chief of staff, Lewis “Scooter” Libby, and George Bush's most valued adviser, Karl Rove, the investigation clearly had the potential to knock the administration into a ditch. As if that were not enough trouble for the president, many conservatives are furious with the White House. Mr Bush's naming of his personal lawyer, Harriet Miers, to the Supreme Court attracted so many conservative brickbats that Ms Miers withdrew her name from consideration on October 27th.

Mr Bush was doubtless surprised, after picking Ms Miers on October 3rd, at just how much his social-conservative base hated the idea of her sitting on the top court. It was not her beliefs that irked them—Ms Miers is a born-again Christian who disapproves of abortion. But she did not appear to come close to the level of constitutional expertise required of a Supreme Court justice. A questionnaire she completed for the Senate Judiciary Committee was sent back because members found her responses “inadequate” and even “insulting”. Two new conservative websites, www.withdrawmiers.org and www.betterjustice.com, were set up to prevent her confirmation.

For social conservatives, the Supreme Court is the crucial battleground. As they see it, liberal activist judges have twisted the constitution to ban prayer in schools and allow abortion-on-demand. Another fight is looming over gay marriage, which judges have legalised in Massachusetts and which social conservatives fear could spread to other states and undermine traditional wedlock.

Until this month, social conservatives were satisfied with the judges Mr Bush had appointed. His picks for lower courts were typically both conservative and well-qualified, as was his first pick for the Supreme Court, John Roberts, now chief justice. In naming Ms Miers, however, conservatives thought Mr Bush had avoided a fight he could have won; Republicans have a 55-45 majority in the Senate, which confirms judicial nominations. With Ms Miers gone, Mr Bush can pick someone who will please his natural supporters. But even if he manages to put the Miers saga behind him, he still has plenty of other problems.

Mr Fitzgerald was due to end his investigation this week. The case concerns the alleged leaking of the name of a CIA agent, Valerie Plame. Since Ms Plame was an undercover agent, albeit one who worked in the unhazardous environment of Virginia, to blow her cover deliberately would be a serious crime. She was first outed in a column by Robert Novak in July 2003. The questions the grand jury must ponder are: who leaked her name to journalists? Did they realise at the time that she was a covert agent, rather than an ordinary one? And has anyone perjured himself or obstructed the investigation, both of which could be cause for indictment?

The background to the case is that shortly before Ms Plame was unmasked, her husband, Joseph Wilson, a former ambassador, derided Mr Bush's claim, in the state-of-the-union address in January 2003, that Iraq had sought to buy uranium in Africa. Mr Wilson had been sent to Niger the previous year by the CIA to investigate reports that Saddam Hussein had sought uranium there. He concluded that he had not, and professed surprise that Mr Bush apparently ignored his report.

A Senate committee later found that Mr Wilson had mis-stated crucial facts in his conversations with reporters. But that will not help the likely targets of Mr Fitzgerald's probe if they are found to have leaked Ms Plame's name to imply that Mr Wilson had got the CIA job for nepotistic reasons.

Judith Miller of the *New York Times*, who served 85 days in jail for at first refusing to testify, now says that Mr Libby told her Mr Wilson's wife was in the CIA. Matthew Cooper of *Time* says that Mr Rove was his source for the same information. The *New York Times* reported this week that Mr Libby first learned of Ms Plame's identity from his boss, Mr Cheney. If Mr Libby and/or Mr Rove are indicted, they will almost certainly have to resign.

Chronology of a scandal

2002

February: Joseph Wilson is asked to go to Niger to check out an intelligence report that Niger sold yellowcake uranium to Iraq.

2003

January: George Bush mentions in the state-of-the-union address that the British government has learned that Saddam Hussein recently sought significant quantities of uranium from Africa.

March 20th: Invasion of Iraq.

July 6th: In a *New York Times* op-ed piece, "What I didn't find in Africa", Mr Wilson writes that he could not verify that Niger sold uranium to Iraq.

July 14th: Robert Novak, a columnist, identifies Mr Wilson's wife, Valerie Plame, as a CIA operative on weapons of mass destruction. Mr Novak names his sources as two senior administration officials.

July 17th: Matthew Cooper and others, on Time.com, write much the same.

Sept. 29th-30th: The Justice Department informs the White House counsel that it has opened an investigation into possible unauthorised disclosures. Counsel informs the president.

Dec. 30th: Patrick Fitzgerald is named special counsel.

Source: AP

There is never a good time to lose one's brain, but Mr Bush has picked a terrible one. Liberals have labelled Mr Rove "Bush's brain" not only to belittle the commander-in-chief's intellect, but also because they recognise his top strategist's brilliance. Mr Rove masterminded Mr Bush's four election victories (two for governor of Texas and two for the presidency), largely by showing him how to energise his conservative base. If Mr Rove goes, Mr Bush will have lost his sheepdog just as his flock is starting to jump the fences.

Social conservatives may be satisfied for now, but fiscal conservatives are bellowing about the deficit. Nativists are growling about immigration. And foreign-policy hawks are shrieking about the mishandling of the Iraq war. All this is far more worrying for Mr Bush than anything Democrats might say about him. If he loses the backing of conservative America, his legislative agenda will wither.

As the toll of American deaths in Iraq topped 2,000 this week, two conservative foreign-policy heavyweights sniped at Mr Bush's handling of the war. Last week, Larry Wilkerson, a former chief-of-staff to Colin Powell at the State Department, claimed that a “cabal” including Mr Cheney and Donald Rumsfeld, the defence secretary, had made decisions in secret and then presented them “in such a disjointed, incredible way that the bureaucracy often didn't know what it was doing as it moved to carry them out.” He said that America would look back in shame at the *carte blanche* given to its soldiers to torture detainees—a timely remark, as the White House tries to have the CIA exempted from new torture rules.

This week the *New Yorker* published comments from Brent Scowcroft, who was national security adviser to the first President Bush, in which he excoriated the neo-con vision of exporting democracy by force. “You encourage democracy over time, with assistance, and aid, the traditional way. Not how the neo-cons do it,” he said. “This was said to be part of the war on terror, but Iraq feeds terrorism.”

On another front, deficit hawks joined the fray. According to Citizens Against Government Waste, a pressure group, Congress approved 13,997 pork projects this year, nearly a tenfold increase in a decade. Mr Bush has yet to veto a single one. Edwin Feulner, president of the Heritage Foundation, called on him to veto all future bills containing pork.

David Keene, chairman of the American Conservative Union, argued that the right used to “swallow policies we might otherwise have objected to because we've believed that [Mr Bush is] trying to do the right thing against sometimes terrible odds. No more. From now on, this administration will find it difficult to muster support on the right without explaining why it should be forthcoming.”

So far, the conservative revolt against Mr Bush is largely confined to the intelligentsia. Ordinary Republican voters feel no great horror about future deficits or the process by which decisions about national security are made. But they may grow more restless if evangelical preachers take against Mr Bush's next Supreme Court pick, or if the situation in Iraq gets worse.

The conservative crack-up is not yet serious enough to ruin Mr Bush's second term. The news from Iraq is not all bad: a new constitution has just been approved, and Saddam Hussein is in the dock. Some congressional Republicans are proposing modest spending cuts, and Mr Bush still has the power to veto bloated bills, if he cares to use it. The Miers mess seems to have been resolved.

But the split between Mr Bush and many conservative intellectuals is “very deep and probably irreparable,” reckons Bruce Bartlett, a former Reagan adviser, who was recently sacked from a conservative think-tank for writing a book called “The Impostor: How George W. Bush Bankrupted America and Betrayed the Reagan Legacy”. And that fury could spread to the grassroots, especially if some of the hopefuls for the Republican presidential nomination make a show of sounding more conservative than Mr Bush on abortion, gay rights or immigration.

If Mr Bush's approval rating sinks—and most polls put it around 40%—he will find it ever harder to make Congress do what he wants. He badly needs to kiss and make up with his base, but that will be hard if his most effective pair of lips is sealed. Mr Rove is unlikely, as lefty comedian Al Franken suggested last week, to be executed for treason. But his political survival is far from assured, and who else could win back the conservatives who think Mr Bush a traitor to their cause?

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The UN's oil-for-food scandal

Naming names

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From The Economist print edition

The Volcker committee's final flourish

Get article background

IS THE oil-for-food scandal finally drawing to a close? This week, a committee headed by Paul Volcker, a former chairman of the Federal Reserve, issued its fifth and final report detailing the scam. It claims that between 1997 and 2003, the Iraqi government sold $64 billion of oil to 248 companies and bought $34.5 billion worth of humanitarian goods. Oil “surcharges” totalling $229m were paid to Saddam Hussein's regime in connection with the contracts of 140 companies, the committee says; the humanitarian kickbacks reached $1.5 billion and were paid in connection with the contracts of 2,253 firms.

The report stresses that many of the companies concerned may not have known about the illegal payments. But it does accuse four international oil traders of “coalescing to dominate” the Iraqi oil market during the final years of Saddam Hussein's regime by dint of paying the surcharges. The four firms—Bayoil Supply & Trading Limited (from the Bahamas), Glencore International (from Switzerland), the Vitol Group (the Netherlands) and the Taurus Group—employed intermediaries to purchase about 60% of Iraqi oil from December 2000 until Mr Hussein's fall in 2003. All four firms have denied knowingly paying the fees.

Last week, federal prosecutors charged Oscar Wyatt, a veteran Texan oilman, with conspiring with David Chalmers, the owner of Bayoil (USA) Inc, the parent of the Bahamas firm, to bribe Saddam's government to obtain oil. Mr Chalmers was indicted in April. Both men have denied the charges. Last month, Vladimir Kuznetsov, a former Russian official in the UN's procurement office, was also charged in connection with the oil-for-food scandal, while in France, Jean-Bernard Mérimée, a former French ambassador to the UN, has been formally placed under investigation on suspicion of having received oil-for-food kickbacks.

Meanwhile, the Senate Permanent Subcommittee on Investigations, chaired by Senator Norm Coleman, has issued its latest broadside against George Galloway. It claims not only that the British MP solicited and received lucrative allocations of Iraqi oil under the UN programme, but also that he “knowingly made false or misleading statements under oath” in denying this when he appeared before the subcommittee in May. Mr Galloway, who rejects the accusations, has now dared Mr Coleman to bring perjury charges against him.

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New Orleans comes back

A Stonehenge of smelly fridges

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But far too many people are looking for somewhere to live

AP

AS RESIDENTS trickle back, they discover a city of abandoned refrigerators. When people fled Hurricane Katrina, they assumed they would be back in a few days and also that the power would stay on. Now, weeks later, they have returned to find iceboxes full of maggots and putrefying chicken. Many of the reeking white behemoths bear slogans scrawled in black marker, some political ("Please send to George W. Bush"), others descriptive ("Harry Potter and the tower of stank").

This Stonehenge of abandoned fridges may amuse New Orleanians who can move back into their own homes. But many others are having trouble finding anywhere to stay in the Big Easy. An acute shortage of housing is hampering efforts to restart an economy that was fragile long before Katrina.

According to Governor Kathleen Blanco's office, some 200,000 housing units in Louisiana are beyond repair. Of these, 160,000 are in greater New Orleans—a huge loss for a metropolitan area that had only 1.3m people before Katrina hit. Many other homes in the city can be fixed but are not yet habitable, so their returning owners need to find somewhere to live. Rents are soaring.

This is having an effect on the economy. Although some local firms have said that they plan to move elsewhere, most seem keen to stay. Shipbuilders, restaurants and shops all want to hire people, but would-be workers have nowhere to live. Retail stores throughout the region are begging for employees, and even fast-food restaurants are offering signing bonuses.

Some of the bigger apartment owners say Ms Blanco aggravated the housing problem by halting all evictions and other legal proceedings until October 25th. Her order was supposed to stop greedy landlords from forcing out their current tenants and jacking up rents, but landlords in New

Orleans say it delayed repairs and kept them from leasing out units abandoned by their former residents.

Others fault the Federal Emergency Management Agency (FEMA). It first provided temporary trailer homes near the workplaces of some big employers, but then scared workers off by threatening to withdraw rent subsidies for the families of any who stayed in the trailers, even if most of the families in question were staying somewhere else. The much-maligned federal agency has changed that policy. But James Perry, executive director of the Greater New Orleans Fair Housing Action Centre, suggests FEMA's rent subsidies themselves are helping to fuel the rush for apartments in and around the city.

The housing shortage has been hard on newly arrived reconstruction workers who know nothing about the geography of New Orleans. “We've been through hell for two weeks,” says Kevin Burkhamer, the co-owner of a Wisconsin excavation firm that is removing debris from one part of the city. He says a government contractor had promised that his crew would get meals and space in a college dormitory. Instead, they ended up sleeping on top of their trailer and on the pavement outside a hardware store. Weary of driving two hours to a truck stop to take a bath, the Wisconsinites rigged up a shower by hoisting a 55-gallon drum of water into the air with a forklift.

Mr Burkhamer, who hopes to stay for two or three years, is hardly alone in his plight; parking lots and median strips have become campsites for rubbish-haulers and demolition crews from across the country. Some locals are happy to donate food to the friendly workers who are carting their trash away, but the influx of contractors and subcontractors unnerves others. Local union leaders worry about work going to newcomers. Mr Perry blames the high rents partly on companies leasing large numbers of apartments for use by out-of-state workers.

In some ways the housing crunch is surprising, because daily life in New Orleans remains inconvenient at best. Telephones and the post work sporadically, most petrol stations and groceries remain closed, and the few restaurants that are open have long waits. During a warm, unusually dry October, there's been little rain to wash away the dust—or the smell—left behind by receding floodwaters. Despite an attempt to “repopulate” the less damaged bits of the city, people have not rushed to move back into their homes, so they stand empty—an irony when so many are looking for places to stay. Still, sales of new refrigerators are brisk.

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Economist.com WORLD NORTH AMERICA

Antonio Villaraigosa

But what's in the enchilada?

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From The Economist print edition

An impressive start, but eventually LA's mayor will have to do something

HE IS just about everywhere in Los Angeles: talking to the derelicts and junkies on Skid Row, riding a new bus line, visiting strife-torn high schools, mediating in labour disputes, operating construction machinery, planting trees, hobnobbing with senators, even appearing in a TV sitcom. If success is defined by visibility, Antonio Villaraigosa, four months into his four-year term as mayor of America's second city, has already won hands-down.

This week, a Harvard University panel, commissioned by *US News & World Report*, named the 52-year-old mayor as one of America's 25 “best leaders”. And in a state where Latinos are a third of the population, Democrats are already talking about him as a future governor. But is this a triumph of style over substance?

A charismatic young Latino who “dares to dream” was always bound to win headlines, especially as he succeeded Jim Hahn, a plodder even by the standards of LA city government. But in the end the new mayor will be judged by how he deals with three barely-tractable LA problems: ghastly public schools, a troubled police force and the most congested roads in the country.

The problems of the Los Angeles Unified School District (LAUSD), the nation's second-biggest with some 700,000 students, are daunting. Just days after his election, Mr Villaraigosa's visit to one high school was marred by fighting between black and Latino students. Close to half the city's eighth-graders (13-14 year-olds) are below basic proficiency in reading.

Clearly, having more students who need to learn English than any other state carries a cost. But there are also structural problems to do with accountability, the teachers' unions and the sheer size of the LAUSD. On the campaign trail, Mr Villaraigosa said he wanted to take control of the public schools, just as mayors had successfully done in Chicago, New York and Boston. In office, he has backed away from the plan, instead forming a panel of teachers, headmasters and education experts to advise him on reform. Cynics note that the teachers' unions, which oppose mayoral control of the school board, were heavy contributors to the Villaraigosa campaign.

A second campaign promise was to add 1,300 new officers within five years to LA's underfunded and undermanned police force (it has just 9,000 cops, compared with almost 14,000 in Chicago). In the 2005-06 budget, which was proposed by the former mayor, Mr Hahn, and approved by a city council which included Mr Villaraigosa, there is money for just 379 more officers this year.

Many experts think LA needs many more police officers, especially to pacify its poorer southern and eastern parts: William Bratton, the police chief who worked wonders in New York, has talked about delivering “the safest large city in America” with 3,000 more cops. The difficulty for Mr Villaraigosa, who has hinted at a special half-cent sales tax for the purpose, will be to persuade Angelenos to pay for more police. After all, most Angelenos who bother to vote live on the Westside or in the northern San Fernando Valley, far from the gang-infested neighbourhoods.

With traffic, one of the mayor's first acts was to appoint himself chairman of the Metropolitan Transportation Authority, which provides mass transit by bus, light rail and subway throughout LA County. This week he showed off a proposed 14-mile dedicated bus-only corridor running east to west along the San Fernando Valley, though the photo-opportunity was somewhat marred when a motorist ran a red light and crossed in front of the sleek new Orange Line bus. Meanwhile, a panel of independent experts has begun to examine one of the mayor's pet projects—a subway line that will stretch, at vast expense, from the centre of Los Angeles westward along Wilshire Boulevard to Santa Monica and the Pacific Ocean.

And to be fair to Mr Villaraigosa, all his running around (250 community events, and 24,000 miles of travel in his first three months) does count for something. One of the problems of being the mayor of Los Angeles is that so few of the city's departments are directly under his control. The bully pulpit offers Mr Villaraigosa his best chance of getting things done. So far, with the possible exception of his cowardice over the schools, he has done a good job of preparing the ground; now one of America's 25 best leaders has to change things.

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Gay marriage in Texas

Brothers in arms

Oct 27th 2005 | AUSTIN
From The Economist print edition

Brace yourself for an unsurprising decision from Texas

WHEN Texas's post-civil war constitution was adopted in 1876, it barred “idiots and lunatics”, not to mention paupers and women, from voting. So it is perhaps reassuring that the document is one of the most-amended state constitutions in the country. But the 434th amendment (or thereabouts) will be a step back in time. On November 8th, Texas will probably become the 19th state to pass a constitutional ban on gay marriage.

Early voting on Proposition 2 began this week. Turnout is likely to be low, since everything else on Texas's ballot this year is virtually unintelligible (unless, that is, you know whether to support a “six-year term for a board member of a regional mobility authority”). The one exception is Houston, where there is a mayoral race. That said, the outcome does not seem in much doubt.

No recent polling data exists, but in 2003 some 70% of Texans believed that homosexuality was wrong. Two years ago, the legislature passed its Defence of Marriage Act, which outlawed civil unions too. Sodomy involving same-sex partners was not even legal until two years ago, when the Supreme Court in *Lawrence v Texas* overturned a law banning it. So delicate are Texan sensibilities that the legislature earlier this year considered banning risqué cheerleading (perhaps a greater threat to heterosexual marriage).

Churches are urging the faithful to go to the polls. One pastor has reportedly compared the fight against gay marriage to the Alamo (both, apparently, are great moral struggles, though the Alamo was surely against worse odds). Fliers have started appearing on Austin windscreens warning eloquently that “Homosexual groups want to pass the same-sex marriage in Texas.” Lest anyone still have doubts about their morality, the Ku Klux Klan plans a demonstration in Austin, the gayest city in Texas, on November 5th.

Homosexual groups are battling back. They have sponsored television ads, showing gays, both male and female, as happy families. Some are even warning that the language of the proposed amendment could have the unintended effect of outlawing traditional marriage. The logic goes like this: if “marriage in this state consists only of the union of one man and one woman” and Texas is barred from “creating or recognising any legal status identical or similar to marriage”, then since marriage is identical to marriage, presumably it will not be recognised.

“Absolutely ludicrous”, scoffs Warren Chisum, a representative from north Texas who authored the proposed amendment. He argues that Texas needs to change its constitution because the 2003 Defence of Marriage Act could take a beating in the courts. “Once you put it into the constitution, it's not subject to challenge in the state court,” he explains.

Mr Chisum is right to be frightened of the courts. Washington state's Supreme Court is expected to rule soon on the constitutionality of that state's 1998 defence of marriage law. Judges remain sympathetic to gay rights, and not just in poncy unTexan places like Massachusetts. In deeply conservative Kansas, the high court ruled last week that sex with under-age children should draw

the same penalty, whether the contact was gay or straight.

Even with a constitutional amendment, Texan manhood might not be safely protected from the liberal judiciary's impositions. This spring, a federal judge struck down Nebraska's constitutional amendment banning gay marriage and civil unions, on the basis that it violated the 14th amendment's equal-protection clause. Hence the continued determination by conservatives to get an amendment to the federal constitution banning gay marriage through Congress. In Washington, DC, Sam Brownback, a conservative senator from Kansas, held some hearings on the subject last week.

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Adult entertainment

Lapping it up

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From The Economist print edition

What price a good time?

IN ITS own way, Scores is just as much a New York institution as the Empire State Building, the Metropolitan Museum and Yankee Stadium. The upmarket lap dancing club is the favourite hang-out for high-rollers nostalgic for the days before former mayor Rudy Giuliani drove the girlie bars out of Times Square. George Clooney held a birthday bash there; Tiger Woods called in (obviously by mistake); Madonna dropped by, pre-Kaballah; sex-jock Howard Stern loves the place so much that its girls appear regularly on his show.

When out-of-towners come a-cropper in Scores, most New Yorkers adopt a position of amused superiority. Last year the papers were full of tales of upright conservatives letting their hair down during the Republican convention. “Not only were the Republicans raucous, they were also naive and provincial,” wrote a hack who took a job there to get her scoop. “Even the nasty ones were compelling—and I thought I had encountered every breed of dirtiness in the preceding month.”

A similar Manhattan smirk greeted the news that American Express is suing a businessman from Missouri over non-payment of what the *New York Post* called a “big bouncing bill” for $241,000, run up during a single night at the club. Robert McCormick, the chief executive of Savvis Communications, a computer networking firm, is accusing the club of fraud. To celebrate completing a deal, he says, he spent a mere $20,000 that night—an amount which, noted various New York comedians, “will make his wife feel much better”. His firm says that he did not try to expense the charge, but he is on unpaid leave.

Whilst the tabloids have revelled in the woes of the “Lap Dunce”, the *New York Times* has groped for higher ground, running an op-ed, which argued that in strip clubs, “paying the price is part of the experience...A reasonably priced lap dance is not a right.” Whether that is so may soon be debated in court, depending on the outcome of a “probe” by the Manhattan district attorney into claims that Scores has frequently overcharged on credit cards, taking advantage of the natural reluctance of customers to complain too loudly. Mr McCormick's is not the first row; in 2004, a Bangladeshi businessman contested a $129,626 charge for five hours at Scores.

Scores denies these accusations, and lists an array of precautions that it takes to ensure that its customers are who they say they are and know what they are spending. These include taking fingerprints and calling the credit-card company for approval for every $10,000 incurred. If so, the latest burst of publicity for such fine customer care may even be good for business. But is it really true? Alas, *The Economist*'s expenses policy did not allow your intrepid reporter to investigate further.

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Rodent news from Gotham

Tails of the city

Oct 27th 2005 | NEW YORK
From The Economist print edition

Things are going well for rats in New York. But not for giant inflatable ones

ARE rodents the only thing between Mike Bloomberg and a second term in Gracie Mansion? The mayor's latest annual report on city management is a glowing paean to the rising quality of life under his rule. Crime is down 5% year on year, violence in jails is down 25%, civilian fire deaths have fallen to the lowest level since 1919—all good news with an election due in November.

The big exception is complaints about rats and mice, which rose 40%, to almost 32,000, in the year to March. Officials blame the jump in reports on the ease with which complaints can now be made through a new City Hall telephone hotline. But many New Yorkers would beg to differ. Anecdotal evidence suggests more rats are being seen in parks and on subway platforms—where, at a foot in length and a pound or more in weight, they are hard to ignore.

One Brooklyn neighbourhood held a “Rat Fair” in a local park this month as a protest against infestation. Things got so bad that “if a kid dropped something, it was lunch”, said one resident. Robert Sullivan, author of a recent bestselling book on New York rats, thinks the much-quoted figure of one rat per New Yorker is an exaggeration. But he warns: “Don't think they are not near you.”

New construction sites, loose garbage, even unusually warm summer weather are variously blamed. This week the city health department convened a three-day “Rodent Control Academy”, the first in a series to sharpen the skills of its exterminators.

One traditional New York solution which, alas, is not open to Mr Bloomberg is to sue the rodents. Going to the courts, however, does seem to work with inflatable rats. American labour unions have long enjoyed tethering such creatures in front of companies they accuse of paying excessively low wages. The first was spotted in Chicago in 1987. Nowadays a union branch office will sometimes have two or three on hand, from 15 to 30 feet long, depending on the scale of the dispute.

The unions insist the rats are a form of “symbolic speech”, protected by the constitution. Employers say they are a form of coercive picketing aimed at turning away suppliers, customers, and other employees, and a violation of the National Labour Relations Act.

Things have come to a head in the Pied Piper dispute. In June, a Long Island court outlawed the use of inflatable rats in a local labour dispute. Now the case moves on to the National Labour Relations Board, probably later this year, and could be subject to further judicial appeal. At worst, that gives the unions plenty of time to order up new balloons in the shape of cockroaches or skunks.

Lexington

Saint Patrick

Oct 27th 2005
From The Economist print edition

Republicans should think twice before trying to demonise the White House's tormentor

THIS Monday's *New York Daily News* printed a delicious bit of character assassination: “He's a vile, detestable, moralistic person with no heart and no conscience who believes he's been tapped by God to do very important things.” No, this was not yet another vacuous actress moaning about George Bush. It was a “White House ally” describing Patrick Fitzgerald, the special prosecutor who is leading the investigation into who leaked the name of a covert CIA agent, Valerie Plame, to the press.

For the past two years the Republican noise machine has been remarkably quiet about Mr Fitzgerald. Now Republicans are starting to crank up the volume against the man from Chicago, accusing him of suffering from an advanced case of “special prosecutor disease”, suggesting that he doesn't know the difference between a legal technicality such as perjury and a real crime, and even suggesting that he has political leanings.

Before they start shouting any louder, conservatives might study what happened to the liberal noise machine when it took on Mr Fitzgerald. Few organs on America's tattered left have as much heft as the *New York Times*, which decided to put the full weight of its authority behind one of its star reporters, Judith Miller, when she refused to divulge her sources to Mr Fitzgerald. Editorials hammered him for mounting a “major assault” on journalistic freedom. Both the editor, Bill Keller, and the publisher, Arthur (“Pinch”) Sulzberger, accompanied Ms Miller to court; and, when she was incarcerated, the newspaper thundered that she was “surrendering her liberty in defence of a greater liberty, granted to a free press by the Founding Fathers so journalists can work on behalf of the public without fear of regulation or retaliation from any branch of government.”

The affair has ended with the *Times* looking as if “the runaway Chicago prosecutor” has reversed over it repeatedly. Not only did Ms Miller end up testifying about her breakfasts with Scooter Libby, Dick Cheney's chief of staff, but the *Times*'s use of its “great liberty” is under attack from all sides. Mr Keller has now circulated a memo accusing Ms Miller of “misleading” her boss about her relationship with her sources and of being “entangled” with Mr Libby. (Ms Miller calls this memo “ugly” and “inaccurate”.) Byron Calame, the paper's public editor, has penned an article entitled “The Miller mess”. In a notably catty column, Maureen Dowd described her colleague as a “woman of mass destruction”—a mild rebuke compared with what *Times* people say in private.

This should serve as a powerful warning to the Republicans. After all, the *Times* could claim it was defending a grand constitutional principle. The White House has fewer options. (The right to leak confidential information to the press? The right to smear a critic of your policies? The right to tell half-truths to a grand jury?) And the Republicans suffer from three handicaps that could turn any campaign against Mr Fitzgerald into a farce.

The first is that they are starting too late. The Democrats began to demonise Kenneth Starr, the special prosecutor in the Lewinsky affair, as soon as he appeared on the scene. The Republicans have been excessively nice about Mr Fitzgerald, who was appointed by a Republican official rather than a panel of judges (as Mr Starr was). James Comey, the deputy attorney-general, introduced Mr Fitzgerald as “Eliot Ness with a Harvard law degree and a sense of humour”. Mr Bush, to his credit (and completely unlike Mr Clinton), has insisted on the seriousness of the inquiry; only the other week, he praised Mr Fitzgerald for handling the case in “a very dignified way”.

Second, Mr Fitzgerald is no Ken Starr. Mr Fitzgerald is as apolitical as Mr Starr was partisan. When he registered to vote in New York, Mr Fitzgerald registered as an independent only to discover that the Independents were a political party, so he changed his registration to “no affiliation” (a label he kept when he moved to Chicago). He is an equal-opportunity prosecutor. In Illinois he is currently embroiled in two big corruption cases—one directed against George Ryan, a former Republican governor, the other against various aides to Richard Daley, Chicago's Democratic mayor. He is repeatedly described by the locals as a “straight arrow” and “a straight shooter”.

Sauce for the goose

Mr Starr, a conservative and a God-fearer who sang hymns on his morning jog, was a ready-made *bête noire* for the left. Mr Fitzgerald embodies everything that conservatives ought to admire. He is the son of Irish immigrants who worked his way through Amherst and Harvard Law School (his doorman father found him work as a doorman). He is a workaholic who made his reputation prosecuting gangsters and terrorists, starting with the Gambinos. (In good Godfather fashion, he even had a witness flown in from Sicily.) He convicted Sheik Omar Abdel Rahman of the 1993 World Trade Centre bombings, travelled to Africa to investigate the embassy bombings of 1998 and brought the first American indictment of Osama bin Laden.

The third handicap for Republicans is that their arguments during the Lewinsky affair may be thrown back in their faces. How can they moan that Mr Fitzgerald has broadened his inquiry well beyond the original leak, when they supported Mr Starr's leap from dodgy land deals to oral sex? How can they say that perjury and obstruction of justice are technicalities when, during the Lewinsky affair, they declared that “perjury and obstruction of justice are high crimes and misdemeanours” (Senator Bill Frist) and that “perjury and obstruction of justice are crimes against the state” (Senator Sam Brownback)?

One of the golden rules of politics is to choose your enemies wisely. So far, Mr Bush has been lucky or skilful in this regard. Mr Fitzgerald is somebody who can do Mr Bush great harm; but conservatives attack him at their peril.

Economist.com WORLD LATIN AMERICA

Argentina

After Kirchner's victory

Oct 27th 2005 | BUENOS AIRES
From The Economist print edition

AP

Following a successful electoral gamble, some hard decisions for the president

Get article background

THE contest between Argentina's current first lady and her predecessor to represent the province of Buenos Aires in the national Senate was billed as “the mother of all the battles” in a mid-term election on October 23rd. When the votes were counted in this Amazonian contest, Cristina Fernández de Kirchner had won a crushing victory, by 46% to 20%, over Hilda González de Duhalde. Across the country, the candidates of Argentina's president, Néstor Kirchner, did almost as well, winning some 40% of the vote. What Argentines will now want to know is what Mr Kirchner proposes to do with his victory and whether it is the prelude to winning a second term in 2007.

Through the vehicle of his wife, the president can claim to have won the two things he wanted from the ballot. The first is a personal mandate from an election in which he was not a candidate. He had been denied such a mandate in the 2003 presidential contest when Carlos Menem, another ex-president, withdrew from a run-off ballot. The magnitude of his victory last weekend was not far short of that achieved by Mr Menem in his first mid-term election, in 1991. His candidates won 15 of a possible 16 senate seats, earning Mr Kirchner a comfortable majority in the upper house. In the 257-seat lower house, they will form by far the largest block, although he will have to negotiate with others, both inside and outside Peronism, to secure a legislative majority.

That task will be made easier by Mr Kirchner's second reason for satisfaction: he can now claim the undisputed leadership of the Peronist movement, no longer having to share this with Eduardo Duhalde, his predecessor. Buenos Aires province, home to 40% of Argentines, has long been Mr Duhalde's turf. Choosing the province as the venue for Ms Fernández's candidacy was a gamble,

but one which paid off spectacularly. Mr Duhalde's congressional block has shrunk from 33 deputies to 25, and will probably decline further at the next election, for president and part of Congress, in 2007. “Kirchner hasn't killed the Duhaldes yet, but now it's a question of when, not if,” says Nicolás Ducoté of CIPPEC, a Buenos Aires think-tank.

But the election also legitimated new opponents. The strongest is Mauricio Macri, a businessman who runs Argentina's most popular football club, Boca Juniors. Mr Macri won the race for the lower house in the city of Buenos Aires, with a margin of a dozen percentage points over Elisa Carrió, a leftish lawyer, and Rafael Bielsa, Mr Kirchner's foreign minister. Mr Macri will now dispute the leadership of the centre-right with Jorge Sobisch, the governor of Neuquén province. Ms Carrió was hurt by a scandal—invented by the government, she claimed—over foreign bank accounts, but her party picked up three seats in the lower house.

Mr Kirchner, a populist nationalist, will doubtless prefer it if his main challenge in 2007 comes from the right than the left. He took office as the economy was recovering strongly from its collapse in 2001-02. He now faces a cloudier economic picture—and some unpleasant decisions that he has hitherto postponed. The biggest worry is inflation, which has crept into double digits. During the campaign, the president blamed price increases variously on Shell petrol stations and supermarkets. Keeping inflation in check probably requires either higher interest rates or allowing the peso to appreciate. Mr Kirchner has supported neither. The government will also have to deal with demands for wage increases from public employees.

A second thorny issue concerns prices charged by privatised utilities, frozen since 2002. Officials say they do not want to increase charges for residential users until 2007. Maintaining that stance may mean forgoing an agreement that would roll over some hefty debt payments to the IMF. The big question is whether, given the president's penchant for economic meddling, sufficient private investment will be forthcoming to maintain high growth.

It would be a mistake to read too much into Mr Macri's victory in Argentina's wealthiest enclave. But if the strongest challenge to Mr Kirchner does come from the right, that will give the president an incentive to tackle these issues. Starting with the selection of a new foreign minister to replace Mr Bielsa, Mr Kirchner's chances of a second term will depend on the decisions he takes in the next few months.

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Hurricane Wilma

Battered by the storm

Oct 27th 2005 | CANCÚN, HAVANA AND MIAMI
From The Economist print edition

A long, expensive clean-up from Mexico to Florida

Reuters

A new ruin in the Yucatán

THE first thing to go was the billboards. They stood no chance against the 225km (140 miles) per hour winds that battered Cancún, Mexico's biggest holiday resort, for nearly two days. Pylons and palm trees followed, snapped like matchsticks. Along the north-east coast of the Yucatán peninsula, some of the glitzy beach hotels were turned into flooded, windowless wrecks before Hurricane Wilma moved on to hurl its fury at Cuba and Florida.

It could have been worse. Only eight people were killed when Wilma hit Mexico on October 21st. The authorities organised the swift and efficient evacuation of tens of thousands of tourists and locals. But they failed to guard against looting: after a brief burst of lawlessness, 140 people were arrested. The emergency shelters were ill-provisioned and overcrowded.

Getting the stranded tourists home was a slow job, hampered by damage to the radar and terminal at Cancún airport. Most had to be ferried by bus to Mérida—three hours away normally, but up to twice that because of flooding. Although foreign embassies organised some extra flights, many tourists faced days of waiting at Mérida's chaotic and overcrowded airport.

In Cancún, electricity will be restored to up to 70% of the city and water to 40% within days, promised Rodolfo García Pliego, a local official. The biggest challenge is to rebuild the tourist infrastructure of Cancún and the nearby coast, which receive some 6m tourists a year. In Cancún, the long strip of beachfront hotels, which provide 40% of the city's jobs, may not be back in action until the new year. Some hotels may have to be demolished. And the storm denuded half of Cancún's beach of sand. Wilma's timing could hardly have been worse: Cancún's high season runs from November to Easter. Further south, hotels on the “Mayan Riviera” were reported to have suffered less damage.

Rebuilding Yucatán will cost $2.7 billion, said Vicente Fox, Mexico's president. He is seeking a $500m loan from the Inter-American Development Bank. Then there is the reputational damage: tourists with memories of days spent in cramped shelters with foul toilets will take some coaxing to return.

Cuba, too, has work to do after Wilma. Its well-drilled civil-defence system meant there were no deaths. But a huge sea surge and 20-foot waves caused coastal flooding, and smashed parts of Havana's sea wall. Half a dozen hotels were flooded, and thousands of seaside dwellings destroyed. It was cold comfort for Cubans that Hurricane Dennis in July was far worse.

By the time Wilma reached Florida, it had renewed its force, killing ten people. Up to 6m residents from Key West to Palm Beach were without power—topping the numbers left in the dark by Hurricane Andrew in 1992. Wilma's winds shattered the glass facades of high-rise buildings in Miami's banking district and of government buildings in Fort Lauderdale. Estimates of damage ran as high as $8 billion. George Bush declared a disaster, releasing federal funds; schools were closed for a week and many businesses too. With Alpha, a tropical storm, triggering floods that killed 15 people in Haiti and the Dominican Republic, this year's hurricane system, already the most damaging in a generation, shows no sign of ending.

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Chile's conservatives

Out in the cold

Oct 27th 2005 | SANTIAGO
From The Economist print edition

The strange failure of the right

Get article background

IN 1999, the conservative opposition came within 32,000 votes of overhauling the centre-left Concertación coalition, which has governed Chile uninterruptedly since the end of General Augusto Pinochet's dictatorship. So the opposition might reasonably have assumed that its turn would come in the next presidential election, on December 11th. Instead, it looks set for a humiliating defeat. What has gone wrong?

Part of the answer is that Ricardo Lagos, the man who almost lost in 1999, has been a far better president than he was campaigner. The economy is growing fast and unemployment is falling. The Concertación, whose members include Christian Democrats and Socialists, has found a telegenic candidate in Michelle Bachelet, who would be Chile's first woman president.

But the opposition's plight is largely self-inflicted. It is made up of two parties. The Independent Democratic Union (UDI) is disciplined, dogmatic and ultra-conservative. Its smaller, moderate partner, National Renewal, is a diffuse outfit. Both parties had been expected to back the UDI's Joaquín Lavín, who ran Mr Lagos so close in 1999. Back then, Mr Lavín, a successful mayor of a prosperous Santiago district, was a fresh face. Now that applies to Ms Bachelet.

As Mr Lavín slid in the polls, National Renewal chose to field its own candidate, Sebastián Piñera, a successful businessman. It hoped that he would push Mr Lavín into third place, force Ms Bachelet into a run-off, and reverse the balance of power in the opposition coalition. Instead, polls suggest that the opposition vote is split down the middle. Ms Bachelet has lost some support to a far-left challenger, but was still well ahead with 42% in a recent poll.

Neither of the right's two candidates seem to catch the public mood. Only a quarter of voters identify themselves as conservatives. The Concertación's grip on the centre ground is not being seriously challenged by either man. It established that grip by embracing the dictatorship's free-market economic policies while giving them a kinder face through social programmes.

The opposition could play up its paternity of Chile's economic success—but that would risk reminding voters of its failure to oppose the dictatorship's abuses. Or it could paint Ms Bachelet as a threatening leftist. But she is as cautious a socialist as Mr Lagos. The irony is that “the greatest achievement of the right is that it no longer matters who governs,” notes Sofía Correa, a historian. “Yesterday's revolutionaries have ended up administering the model that best suits the right.” Maybe so, but Chile's conservatives haven't won a presidential election since 1958. The longer they have to wait, the more fractious they are becoming.

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The Latinobarómetro poll

Democracy's ten-year rut

Oct 27th 2005
From The Economist print edition

Latin Americans do not want to go back to dictatorship but they are still unimpressed with their democracies

IF ANYONE ever imagined that building strong democracies in Latin America would be a swift and easy task, this year's Latinobarómetro poll should disabuse them. Economies have been growing strongly across the region and governments are spending more than ever on social programmes, but the poll—taken in 18 countries and published exclusively by *The Economist*—suggests that only about half of Latin Americans are convinced democrats and only one in three is satisfied with the way their democracy works in practice. Those figures have remained almost identical for three years in a row—and are down on those of a decade ago.

This year's poll points to a slightly sunnier mood: political institutions are a little less reviled and presidents are still quite popular even though many are nearing the end of their term. Respondents are slightly more optimistic about their economic prospects, and a bit less hostile towards the United States. They are even starting to warm again to privatisation.

Latinobarómetro, a Chilean organisation, has carried out similar surveys each year since the mid-1990s. So the poll has captured shifts in opinion in the region during a decade that saw initial enthusiasm for democracy and free-market reform tempered by recession (severe in places), and followed by the advent of leftish governments and then a strong economic recovery. Through this switchback, says Marta Lagos, Latinobarómetro's director, what is striking is the underlying stability of opinion.

The disappointments of democracy

1

Which of the following statements do you agree with most? %

	Democracy is preferable to any other kind of government					In certain circumstances an authoritarian government can be preferable to a democratic one				
	1996	2001	2004	2005	*Change since 1996*	1996	2001	2004	2005	*Change since 1996*
Venezuela	62	57	74	76	*14*	19	20	11	11	*-8*
Mexico	53	46	53	59	*6*	23	35	14	13	*-10*
Chile	54	45	57	59	*5*	19	19	14	11	*-8*
El Salvador	56	25	50	59	*3*	12	10	10	4	*-8*
Nicaragua	59	43	39	57	*-2*	14	22	10	10	*-4*
Uruguay	80	79	78	77	*-3*	9	10	7	10	*1*
Argentina	71	58	64	65	*-6*	15	21	20	17	*2*
Costa Rica	80	71	67	73	*-7*	7	8	7	8	*1*
Ecuador	52	40	46	43	*-9*	18	23	30	18	*0*
Honduras	42	57	46	33	*-9*	14	8	11	10	*-4*
Brazil	50	30	41	37	*-13*	24	18	18	15	*-9*
Colombia	60	36	46	46	*-14*	20	16	12	11	*-9*
Bolivia	64	54	45	49	*-15*	17	17	19	19	*2*
Guatemala	50	33	35	32	*-18*	21	21	11	17	*-4*
Panama	75	34	64	52	*-23*	10	23	8	12	*2*
Peru	63	62	45	40	*-23*	13	12	20	20	*7*
Paraguay	59	35	39	32	*-27*	26	43	39	44	*18*
Dominican Republic	na	na	65	60	*na*	na	na	11	15	*na*

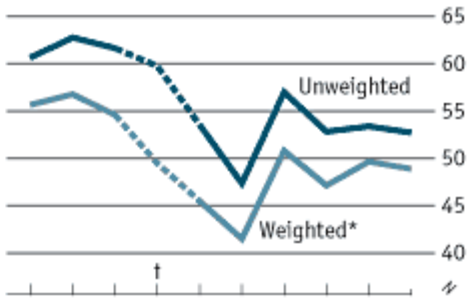
Source: Latinobarómetro

Ranked by increase in support for democracy since 1996.

Weighed down

2

Democracy is preferable to any other kind of government, % agreeing, Latin American average

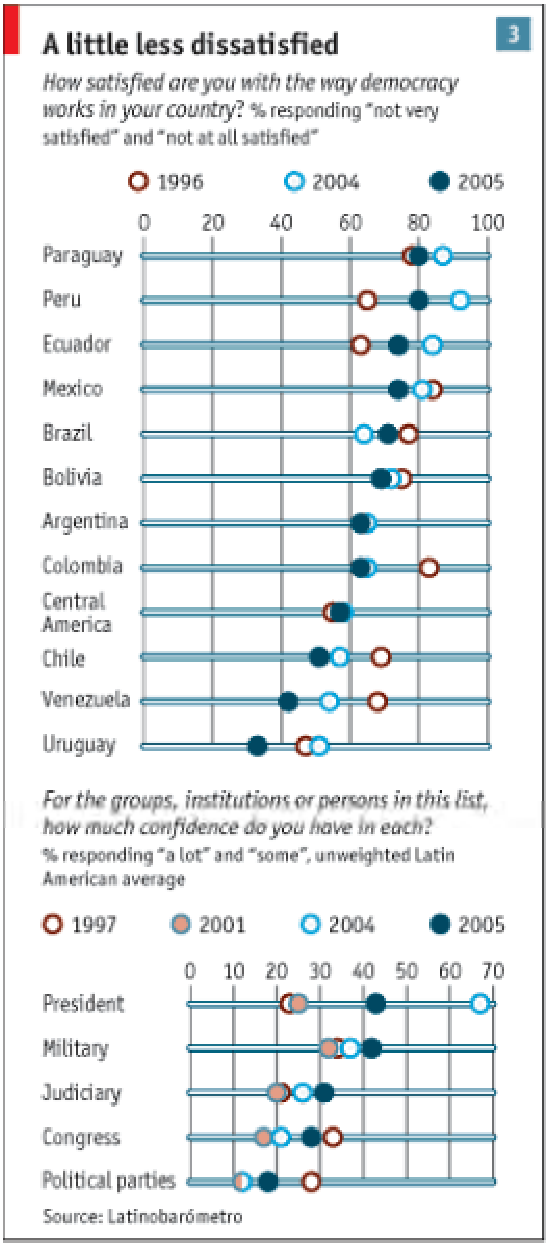


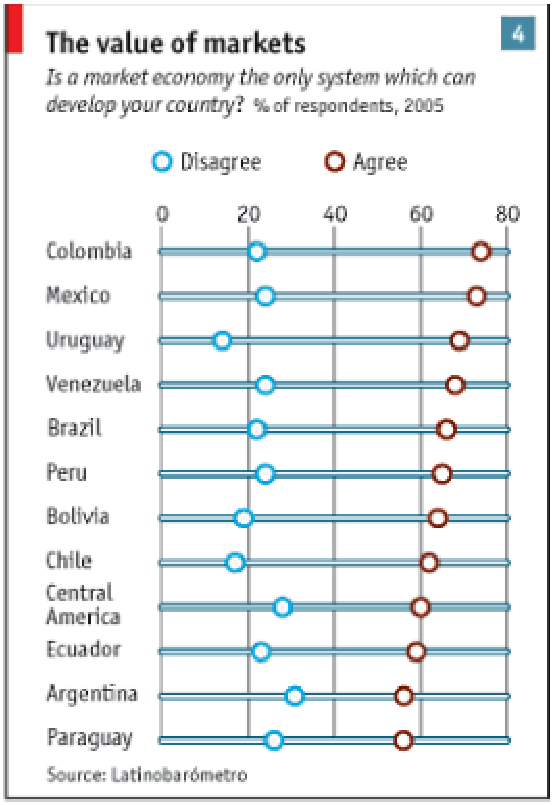
*By 2005 population †No data

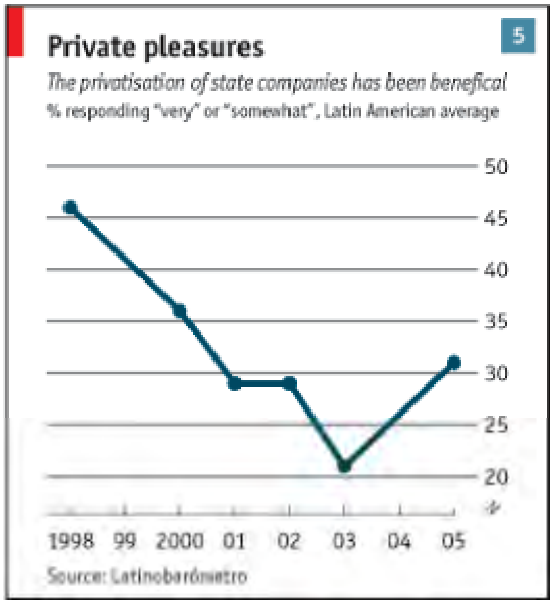
Sources: Latinobarómetro; EIU

Support for democracy is lower in a dozen countries today than in 1996 (see charts 1 and 2). It is worryingly low in Peru, parts of Central America and Paraguay (the only country with a strong authoritarian streak). In Brazil, some of the shine brought by the election of Lula da Silva in 2002 appears to have been removed by a recent corruption scandal involving his party. On the other hand, support for democracy is very high in Venezuela, perhaps because both supporters and opponents of Hugo Chávez, the socialist president, claim it as their banner. It is high, too, in two small countries, Uruguay and Costa Rica, which many political scientists say are the region's only “consolidated” (ie, fully fledged) democracies. It is rising in Chile (which many would say now qualifies for the “consolidated” tag) and in Mexico. But only in Uruguay and Venezuela are a majority of respondents satisfied with the working of democracy (see chart 3).

Nevertheless, the poll suggests a growing resilience in Latin American democracy. Some 62% say that in no circumstances would they support a military coup (though only 51% in Ecuador, 49% in Peru, and 31% in Paraguay). And 70% agree with the Churchillian notion that whatever its problems, democracy is the least bad system of government.



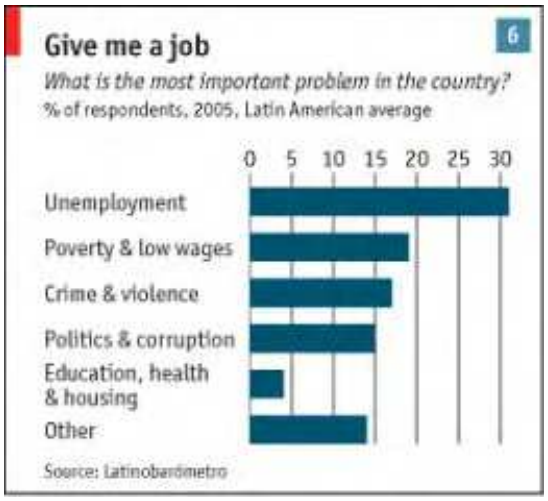




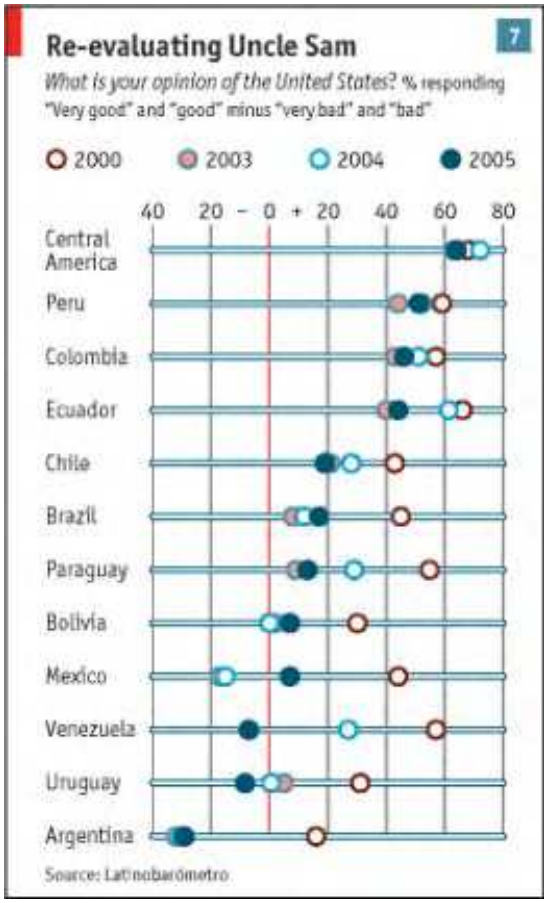
But much of the machinery of democracy is missing or defective. Only 26% of respondents said that citizens in their country are equal before the law—the same number as in 1998. Only a fifth express much faith in political parties and only a quarter in the Congress and the courts—though in both cases that is a slight improvement on recent years (see chart 3). In some countries, mistrust of political institutions has led citizens to take to the streets—in Bolivia, where protests have toppled two presidents in as many years, 11% of respondents said they had taken part in roadblocks and another 12% said they might do so.

The poll shows that a clear majority believe that a market economy is the only means by which their country can develop (see chart 4). Sentiment towards privatisation is improving—perhaps, Ms Lagos suggests, because more people appreciate the service improvements delivered by privatised utilities now that they have a bit more money with which to meet their bills. Latin Americans continue to see their main problems as being unemployment, crime and poverty (see chart 6). Just 31% (up from 27% last year) think their country is progressing. Only in Chile and Venezuela do a majority see progress. But across the region, expectations are rising: 54% think their children will live better than they do, up by 4% compared with last year.

Almost everywhere, opinions towards the United States are thawing, though they are yet to reach the warmth of the late 1990s (see chart 7). There are two exceptions. One is Venezuela, where Mr Chávez accuses (without proof) the United States of planning to invade his country. The other is Uruguay, where a left-wing government took power this year. The most anti-American country remains Argentina, which has long had difficult relations with the United States (except for an interlude in the 1990s). In many other countries, respondents thought that relations with the United States were becoming closer. That may be because the memory of the Iraqi war, which was very unpopular in Latin America, is fading. Central America, with which the United States this year enacted a free-trade agreement, is the most pro-*Yanqui* part of the region.



The most popular leader among Latin Americans seems to be Brazil's president, Lula da Silva, despite his party's recent woes (see chart 8). However, fewer than 50% of respondents expressed an opinion about Lula. Mr Chávez is more popular than his mentor, Fidel Castro, and his arch-enemy, George Bush. But the appeal of *chavismo* in the region may be more limited than is often claimed. Only in the Dominican Republic, a generally pro-American country, did more than 10% of respondents choose Venezuela as the Latin American country they most trusted; in Bolivia and Ecuador, two countries seen as vulnerable to Venezuelan influence, only 5% and 9% did respectively. And the poll suggests that most Latin Americans place themselves in the political centre.



The poll also indicates that crime remains a big problem in the region. Some 41% of respondents said they knew someone who had been a victim of crime in the past 12 months—up from 33% last year. But 30% think progress is being made in reducing corruption in their country, up from 26% last year. The poll also reveals the steady rise of Protestantism in the world's most Catholic continent. In 1995, 80% of respondents said they were Catholic and only 3% Protestant. This year, those figures were 70% and 15% respectively.

After a decade of polling, two things are clear. Latin Americans will not easily revert to authoritarianism, even in hard times. But on the other hand, building consolidated democracies amid poverty, inequality and a legacy of past undemocratic practices, is a long, slow job.

Latinobarómetro is a non-profit organisation based in Santiago, Chile, which has carried out regular surveys of opinions, attitudes and values in Latin America since 1995. The poll was taken by local opinion-research companies in 18 Latin American countries, and involved 20,209 interviews in August and September 2005. The average margin of error was 3%. Central America in the charts refers to Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, Panama and the Dominican Republic. Further details from www.latinobarometro.org.

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Economist.com WORLD ASIA

Kashmir's earthquake

A race against winter

Oct 27th 2005 | ISLAMABAD AND PANJ KOT
From The Economist print edition

AP

As a second disaster looms, the government's critics find their voices

FROM a helicopter above the rugged valleys of Pakistani-controlled Kashmir, the logistics look almost impossible. Hillside after hillside is dotted with the corrugated-iron roofs of inaccessible homesteads. The roofs survived the earthquake on October 8th. But beneath is nothing but rubble. Here and there white stones spell out big “H”s. Hopeful villagers have improvised helipads.

Even now, untold thousands have not been reached by the relief effort. Many are in places where helicopters cannot land and roads have vanished under landslides. Supplies have to be dropped, or lugged on the backs of soldiers and mules. The village of Panj Kot, just 2km (1.2 miles) from the “line of control” dividing Kashmir's Pakistani- and Indian-controlled parts, is eight hours' walk from the nearest market. About 250 of its villagers died in the earthquake, including more than 80 children at school.

The earthquake is known to have killed more than 54,000 people in Pakistani Kashmir and the neighbouring North-West Frontier Province (NWFP), and 1,400 on the Indian side. The big worry now is what happens to the people in the hills as winter sets in and the snow starts falling in November. The United Nations has given warning that tens of thousands of people might die.

The badly injured have already reached help—or have died. Others have left to seek refuge in the tented camps that are springing up near the towns. But some are resisting government appeals to move. For poor subsistence farmers, land, no matter how marginal, is all they have. Mohammad Bashir, a mason in Panj Kot, lost 19 members of his extended family, two of his three cows, and a house he had spent three years building. But with his 12 surviving family members, he feels they are too many to move.

A “secondary” humanitarian disaster is now feared if not enough is done in the next three weeks or so to prepare such people for the winter, and over the following months to help them survive it. Thereafter, rebuilding might take ten years and $5 billion. The priority now is shelter. Of 3.3m homeless, some 800,000 are thought still to be sleeping in the open. There have been hundreds of aftershocks, so even where buildings are standing, people are scared to sleep in them. World stocks of “winterised” tents, some 200,000 of which should have arrived by the time the snows come, are exhausted.

In many places they are not suitable. In Panj Kot, villagers have retrieved beams from their houses, and rigged up shelters with the metal roofs. But these will not withstand Kashmir's winter either. Last year, the village was under 1.5 metres (5 feet) of snow in December and January. Already the mountain tops are white.

The immediate need in Panj Kot, however, is food. The first food drop came only on October 20th. It provoked a big fight. Villagers had stocked up for Ramadan, but stores are near depletion. Overall, an estimated 1m people need food aid now, and many will need it through the winter.

In built-up areas, water and sanitation systems have been shattered, so some 4m people are defecating in the open, giving a high risk of an outbreak of disease. Many of those who survived the quake with relatively minor injuries are in danger. Untreated wounds are turning septic and gangrenous, and there have been a few cases of tetanus. Children are especially at risk. Many now line roads, begging. Some are orphaned; others are their parents' best hope of winning sympathy.

By October 26th, the date of a donors' conference in Geneva, the United Nations' emergency appeal had raised only $90m, of about $550m it said it needed at once (about one-fifth to be spent on using helicopters). Another $580m was promised, but most will arrive too late. “Money can buy everything we need,” pleaded the UN's humanitarian co-ordinator in Pakistan, Jan Vandemoortele, “the one thing money can't buy is time.”

The blame game

Some Pakistanis are criticising America for not having done more, although it has sent some helicopters and promised money. Aitzaz Ahsan, an opposition senator, says he told the American ambassador that the United States had missed a great chance to win hearts and minds. The area around Balakot and Mansehra in NWFP, devastated by the earthquake, was “the very crucible” of

Islamist extremism in Pakistan, and hence a source of enemy recruits in the “war against terror”.

Like many others, Mr Ahsan is also damning of the handling of the relief effort by the government and the army. Some helicopter crews, and medical and engineering units, have performed heroically. But, partly thanks to the scrutiny of Pakistani newspapers and, especially, television, the army command is now under fire. It was slow to recognise the scale of the disaster and to respond to it, and was guilty, says Mr Ahsan, of “colossal mismanagement” of aid distribution.

Samina Ahmed, of the International Crisis Group, a research and lobbying organisation, says the army has only itself to blame, having centralised the relief and rehabilitation efforts under its own command. “It assumes it can do everything better than the civilians. This self-confidence is going to sink it.” Others give it more credit. Mike Penrose, of International SOS, a medical and security firm, who was in Pakistan as a consultant to aid donors, says the army was “way ahead of the international community”.

Co-ordination is complicated by the large numbers of charities and individuals involved. Distrust of the government is such that many prefer to make donations privately. Some relief supplies have found their way on to the market. Others—inappropriate gifts of old clothes—are fuelling campfires. Some supplies donated by Pakistani émigrés in New York and elsewhere are still in distant warehouses. PIA, the national airline, which was to have shipped them free, lacks the capacity to do so.

The political truce in Pakistan that followed the earthquake was short-lived. General Pervez Musharraf is now under fire from both secular and Islamist opponents. One member of the National Assembly from his own party said the quake was “God's wrath” for Pakistan's help in America's invasion of Afghanistan. Many commentators recalled that failures after the cyclone in East Pakistan in 1970 helped lead to the territory's breakaway as Bangladesh the following year. The *Friday Times*, a weekly newspaper, noted that in Algeria, Egypt and Turkey insensitive handling of quake disasters led to a groundswell of support for Islamic parties.

Presumably aware of this danger, General Musharraf has praised the job being done by Jamaat-ud-Dawa and the Al-Rasheed Trust, two Islamist groups in the forefront of the aid effort. These groups are, he says, legal, if on a “watch list”. However, many of their activists were members of banned militant organisations. Their expansion into the vacuum left by the collapse of civilian administration in many places worries liberal Pakistanis.

It will also worry India. It blames the Islamist groups for stoking the insurgency against its rule in part of Kashmir—a conflict which has cost perhaps 80,000 lives in the past 15 years, and which has seen militant attacks and counter-insurgency killings in Indian Kashmir even since the earthquake. Hope has flickered that the earthquake might advance India's peace process with Pakistan, by bringing about a softening of the line of control. General Musharraf says that Kashmiris should now be allowed to cross it.

India agrees, in principle, and has prepared three medical camps along its side of the line. Pakistan has suggested five crossing points. But Pakistan says India's proposal, which requires the patients to return to Pakistan-controlled territory overnight, is only practical for the healthy. Talks are to be held on October 29th, covering issues such as travel documentation.

But there are limits. Neither India nor Pakistan is in a hurry to fulfil its promise to allow Kashmiris to visit their families and do relief work on the other side. Both countries have security concerns, which apparently override humanitarian ones. Yasin Malik, a separatist leader from Indian Kashmir, this week visited some rubble on the Pakistani side, once the town of Balakot. He appealed to India to allow Kashmiris to come and go: “Politics must take a back seat.” In Panj Kot, which, until a ceasefire two years ago, was often under Indian shellfire, Mr Bashir is sceptical. “A

lot of talk and nothing has happened.”

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Nepal

The inland ocean

Oct 27th 2005 | KATMANDU
From The Economist print edition

Katmandu is more vulnerable than most

BISHNU SHRESTHA sells earthquake survival kits, to foreigners mostly, and he admits that he can't see much point in them. The aid-workers and diplomats who come to his shop to buy ethnic bedspreads and crockery occasionally part with $48 for a tin trunk containing a crowbar, plastic sheeting, bottled water and medicine, but there have been no extra sales since the Kashmir disaster. “I think in Katmandu it's not necessary,” he says. “There's no reason for it.” If only that were so.

Katmandu suffers a major earthquake roughly every 70 years and the last one was in 1934. According to Amod Dixit of the National Society for Earthquake Technology, a quake of the same magnitude today would leave 40,000 dead and 100,000 needing hospital treatment. He says 93% of buildings in the city of nearly 2m people do not meet building standards. A new building code for public structures was made mandatory three years ago, but has not been enforced. Meanwhile, the city continues to grow at 6.5% a year.

Two special factors combine to make Katmandu particularly vulnerable. The soil of the valley in which it sits is an ancient lakebed that produces high-intensity vibrations during a quake. In 1934 it was seen to undulate “like the waves of the ocean”. Perhaps even more serious, the city is linked to the outside world by only two mountain roads, which are frequently blocked by landslides when it merely rains, and by a single runway. The roads, though not, with luck, the runway, would be knocked out by a quake of any size.

Geologists have identified an area of western Nepal from Pokhara to Dehradun in India as a “seismic gap” where energy has been building up for at least 200 years. Yet Katmandu's residents frequently treat the subject as a laughing matter. One says that when her family built an earthquake-resistant house they were jeered at for going to the extra expense. Mr Dixit has the same experience when he visits building sites to suggest structural improvements: making a building more secure adds about 3% to the cost of construction. “There is initial resistance and at least half of them think we are funny,” he says. “But once they listen they want to hear more.”

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China

Faintly Declining Investment

Oct 27th 2005 | BEIJING
From The Economist print edition

The torrent of cash heading for China shows signs of abating

ITS rapid emergence as one of the world's biggest recipients of foreign direct investment (FDI), even briefly surpassing America two years ago, has been a source of enormous pride to China's leadership, and a cause of enormous envy to many of its neighbours. So how much should the Chinese worry about signs that inflows this year are levelling off?

The commerce ministry says that FDI in the first nine months fell by 2.1% compared with the same period last year. Many economists predict that, for the whole year, the inflow will be slightly down on last year's record $60.6 billion. This would be the first such drop since 1999 and end a period in which investment has grown annually at a double-digit clip (except, thanks to the SARS respiratory disease, for a puny 1.4% in 2003). Last year's inflow was 13.3% higher than in 2003.

Given the sheer scale of FDI flows—the cumulative total by the end of last year had reached $562 billion—few expected such rates to continue for many more years. The floodgates were opened by China's entry into the World Trade Organisation in 2001. That lowered barriers to investment and trade. Ironically, given the foreign complaints aroused by China's trade surpluses with developed countries, 63.3% of China's export growth last year was produced by foreign-invested enterprises, up from 56.8% in 2000.

What may now be starting to slow is the practice of moving labour-intensive factories to China to manufacture products for export. Taiwan, one of the biggest investors in China, has already moved so much of its electronics production to the mainland that it now makes only the highest-technology components at home. Unless the Taiwan government takes further steps to liberalise hi-tech investments in the mainland, which it restricts for political reasons, the rush could be over.

A saturation of investment, both foreign and domestic, in some Chinese industries may be acting as a deterrent. Intense price competition and rising raw-materials prices have cut profit margins. Last week Volkswagen, a big investor in China's carmaking industry, announced that it would cut investment plans for the period between 2006 and 2008 by 40%. The German manufacturer has suffered a serious erosion of its market share and profits in China as a result of an upsurge of investment by competitors.

This is not wholly bad news for China, which has been trying to curtail investment in overheating sectors. It would be happy to see less investment in property, for example. Last year the property sector accounted for nearly 10% of total FDI inflows, the biggest destination for foreign

investment after manufacturing (71%). FDI inflows into property remains relatively strong but utilised foreign investment last year in the cement industry, which China has also been trying to cool, fell by 67%.

But even if double-digit FDI growth is a thing of the past, the desire to invest in China is hardly going to dry up any time soon. Investment for supplying China's domestic market will take up some of the slack. The Economist Intelligence Unit, a sister company of *The Economist*, forecasts continuing growth in FDI to the end of the decade after a decline this year, albeit at diminishing rates. Some investors worry that the corporate-tax rate might increase to align the rate paid by foreign firms with that levied on domestic firms. But Arthur Kroeber of the *China Economic Quarterly* says that this is unlikely to happen right away.

Despite reports of upward pressure on labour costs, no convincing evidence suggests that China is about to lose its comparative advantage in labour-intensive industries. Profitability has suffered recently, and there are many complaints about the protection of intellectual-property rights, corruption and the murky regulatory environment. But surveys still suggest that investors rate China highly. The UN Conference on Trade and Development said last month that 87% of multinationals it surveyed ranked it the world's most attractive place to do business.

In the first nine months of this year, the value of new contracts signed but not yet implemented rose by 22%. This figure is notoriously unreliable as an indicator. In September alone, however, actual FDI was up 3%. The “bottom line”, says Jonathan Anderson of UBS, a bank, is that China will continue to attract around $5 billion a month. It can hardly complain.

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Economist.com WORLD ASIA

Aceh

Hope is fragile but still alive

Oct 27th 2005 | BANDA ACEH
From The Economist print edition

Amazingly, the post-tsunami peace agreement is holding

Get article background

TWO months into a peace process that is seeking to end a 29-year insurgency is a presumptuous moment to start being euphoric. But unexpected optimism is the overwhelming emotion in Aceh, the tsunami-ravaged province on the Indonesian island of Sumatra where the Free Aceh Movement (GAM) and the government have already advanced much further down the path to sustainable peace than on any of their previous attempts.

This week both the Indonesian security forces and GAM met their latest deadlines, respectively to withdraw troops and hand over weapons. GAM has now given up more than half the 840 firearms it promised to surrender and the Jakarta government has pulled out more than 15,000 soldiers and paramilitary police, a similar proportion of its obligation.

Equally heartening is that there has been only a handful of violations of the agreement signed in Helsinki on August 15th, and neither side has tried to make political capital from them. Strong leadership from both sides, a new-found restraint within Indonesia's hitherto notoriously ill-disciplined army and firm monitoring from 227 observers sent by the European Union and Indonesia's neighbours have set a tone that should maintain momentum. The Acehnese are, for the most part, warmly welcoming home former fighters, while the security forces have all but ended their patrols.

President Susilo Bambang Yudhoyono still faces challenges, most notably to enact promised legislation giving Aceh an exceptional degree of autonomy. His predecessors' failure to carry out such commitments fuelled the original rebellion; he now has 18 months to pass the law and is expected to prolong the drafting process for as long as possible.

Meanwhile, however, government apathy towards nearly autonomous Aceh is growing. President Yudhoyono recently berated the rest of the world for failing to honour its tsunami promises. Although accurate, this was hypocritical. His bureaucracy, particularly the finance ministry, is showing little sense of urgency or desire to rebuild the region that bore the brunt of the December 26th disaster. And the majority of district administrations in Aceh cut their public-services budgets in 2005. If Indonesia doesn't get this rebuilding right, there is still every chance that the peace could go wrong as well.

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Japan and America

No home where the dugong roam

Oct 27th 2005 | HENOKO, OKINAWA
From The Economist print edition

The future of America's security policy in the region pivots on one little beach

EPA

Make waves, not war

Get article background

SITTING bare-footed and cross-legged under a makeshift awning, Teruo Onishi, a retired schoolteacher and peace activist, looks across from the beach at Henoko to an islet with a shrine to welcome the sea gods that look after this part of the world, and a coral reef beyond. He delivers a history lesson. Though the arrival at Japan's shores in 1854 of Commodore Matthew Perry's "black ships" may, with good reason, be better known to Japan and the world, says Mr Onishi, it is the earlier, friendly visit to Okinawa of a British naval captain, Basil Hall, in 1816 that is remembered by locals.

Okinawans took to Hall, allowing him to land and even to bury one of his crew—the grave may still be seen. On his voyage back to England, Hall called on Napoleon on St Helena. He spoke warmly and at length of the Ryukyu archipelago (then known as Loo-Choo, which now makes up Japan's Okinawa prefecture). When, Hall wrote later, he recounted how the Okinawans had no "wars or weapons of destruction", Napoleon was amazed.

Today, few spots in the world are as heavy with weapons of destruction as Okinawa, and they are American: this southernmost of Japan's prefectures is home to half the 50,000 servicemen America maintains in the country. After a teenage girl was raped in 1995 by three of them, America agreed to close its most deeply resented facility on Okinawa—Futenma air base, its biggest overseas marine base, squeezed right up against crowded Ginowan city. But first, an alternative had to be found.

America proposed building a floating heliport 1.5 miles (2.5km) long over the coral reef at Henoko, on Okinawa's eastern side. The Japanese government turned down the site, where

dugong, a rare sea-cow, graze. Instead, it proposed that the heliport be built on land near Henoko, where America's Camp Schwab now sits. This time the Americans objected. Not only would that cramp the marines' training, they said; there were also villages about, and the whole point of relocating was to escape local residents' objections to noise and danger.

Nearly a decade after the negotiations to move Futenma began, a sense of urgency has been growing. Occasional rapes, assaults and traffic accidents committed by American servicemen still arouse resentment. Last year a helicopter crashed on a university campus in Ginowan. Both America and Japan are now keen to have something to show for a planned summit between George Bush and Japan's prime minister, Junichiro Koizumi, in mid-November, when Mr Bush may also visit Okinawa.

This week the Americans' frustration erupted over the lack of progress. Richard Lawless, deputy assistant defence secretary for Asia and the Pacific, said in Tokyo that the security alliance with Japan, the foundation of America's security policy in Asia, was being undermined by “interminable dialogue over parochial issues”. That outburst seemed to do the trick. For on October 26th a deal appeared to have been reached. This would involve building a heliport with a shorter runway, partly on Camp Schwab land and partly running into the sea.

This will supposedly save the dugong's grounds and keep flights farther from residential areas. Ending the rift with Japan will also help the Americans to overhaul their security strategy in East Asia, giving them more flexibility to deal with the threats posed by terrorism, by a nuclear-armed North Korea, by the military muscle of a rising China and, with that, the potential for conflict over Taiwan. With the base row over, if America can rely upon Japan to play a greater part in its own defence, America can reduce the number of its own troops in Japan and move some forces to Guam or even Hawaii.

First, however, the deal over the relocation of the Okinawa air base has to satisfy the people of the island, and the politics is tricky. For a start, the governor, Keiichi Inamine, a proud man, has blessed the offshore heliport scheme and appears unwilling to lose face. As for the electorate, anti-military feelings are high. It is not just that Okinawa, with 0.6% of Japan's land area, has long had to bear a disproportionate brunt of the American presence. History still plays a powerful part: some of the bloodiest campaigns anywhere in the second world war were fought in Okinawa, and a third of the civilian population died. America did not return Okinawa's sovereignty to Japan until 1972, and feelings of second-class citizenship linger.

On the other hand, the bases' presence brings lashings of central government money to the country's poorest prefecture. On top of a cornucopia of grants, subsidies and tax concessions, the government pays the salaries of the 8,800 Japanese who work in the bases. Okinawans on whose land the bases are built are paid ¥80 billion ($670m, or over $100,000 a hectare) in rent a year. These landowners, of whom there are 29,000, are in no hurry to see the Americans go. With a key mayoral race in Nago, near Henoko, next January and a governor's race later in the year, regional security might yet have to wait.

Syria and the Hariri assassination

High noon in Damascus

Oct 27th 2005 | BEIRUT
From The Economist print edition

Syria's government is in the dock over the murder of Lebanon's Rafik Hariri

Get article background

A TONNE of high explosives can cause a lot of damage. For instance, the giant blast last February that targeted Rafik Hariri, Lebanon's best-known politician, also killed 22 others, injured scores more and turned a posh stretch of Beirut's seafront into a scorched, pockmarked moonscape. That particular bomb continues to resound far and wide: and nowhere more so than in the Syrian president's clifftop palace overlooking Damascus.

The latest reverberations come from a report into the bombing by UN investigators which points a tentative, but persuasive finger of guilt at top figures in the Syrian government, including President Bashar Assad's brother, Maher, and his brother-in-law, Asef Shawkat, who head respectively the presidential guard and intelligence services. Responding to the report, the Security Council is debating a resolution that would oblige Syria to co-operate more fully with the investigators, whose mandate has been stretched to mid-December. Failure to surrender suspects could lead to punitive sanctions.

Evidence of high-level thuggery was already strong enough for Lebanon to have arrested four senior security chiefs who were, essentially, Syrian clients. The implication of more direct Syrian involvement now threatens not just embarrassment, but diplomatic isolation and a roll-back of Syrian influence that could transform the whole region.

Most observers dismiss as unlikely an outright collapse of the regime. Internal opposition to the ruling Baath Party remains weak. Underground opposition groups are small, divided and closely

watched. Outside powers are wary of destabilising the country, fearing that Syria's complex ethnic and religious mix could prove as combustible as Iraq's. Even Israel thinks a weakened Syria better than a failed state or an Islamist alternative.

A weakened Syria would be hard-pressed to maintain its shadowy but crucial support for such causes as radical Palestinian groups, the Iranian-backed Hizbullah militia in Lebanon and the Sunni insurgency in Iraq. This is why America, in particular, is keen to keep Syria under pressure. And such pressure has already brought results. Syria's border with Iraq is better sealed, despite American and Iraqi protests that jihadists continue to cross. Only last week, Syrian intelligence furtively deported a nephew of Saddam Hussein's who is believed to have been a key figure in funding the insurgency. But American officials describe such gestures as too little, too late.

Most Lebanese have long suspected their neighbour over the Hariri killing and other crimes. That is why a million of them took to Beirut's streets last March, in a peaceful uprising that led to the ouster of Syrian troops and the Lebanese regime they propped up. It was Syria, of course, that held sway in Lebanon for 25 years, following a desperate plea for troops from its smaller neighbour's then-besieged president to save his neck during his country's then-escalating civil war.

But Syria, as the UN report makes clear, grew rather too comfortable with calling the shots in Lebanon (often literally) and with raking in profits from its casinos, banks and utilities. Last September, Syria's president bluntly ordered Mr Hariri, then Lebanon's prime minister, to back an unusual three-year extension in the term of office of Lebanon's pro-Syrian president, Emile Lahoud. Mr Hariri eventually resigned over the issue, and put his considerable charm and $5 billion fortune at the service of a budding opposition movement. His death came just weeks before elections that this movement appeared likely to win.

The case for the prosecution

The UN report, compiled by a German prosecutor, Detlev Mehlis, presents this background in telling detail. Having established a motive, it goes on to describe a range of incriminating evidence. Most compelling are mobile-phone records that reveal the existence of a wide-ranging conspiracy to eliminate Mr Hariri. These include not just records from a set of callers, linked to the Lebanese and Syrian intelligence agencies, in the immediate vicinity of the crime. One caller, an official in a Syrian-backed Lebanese Islamist sect known as the Ahbash, put in a mysterious direct call to Lebanon's president only minutes before the blast.

The most damning evidence, however, is more controversial. Mr Mehlis cites two Syrian witnesses as having actually observed the preparation, in a Syrian camp, of the car bomb used for the assassination. But one of these witnesses is a Syrian defector with a history of telling tall tales. He is now being held in France, not as a witness but as a suspect in the murder. Syria has seized on such inconsistencies to challenge the legitimacy of Mr Mehlis's report, claiming that the investigation has been politicised.

Despite such bluster, Syria has declared that it will continue to co-operate with Mr Mehlis's investigation. One possibility, which has been raised by both the prosecutor and the Syrians, is for the country to mount its own investigation. With the already vocal backing of Russia, and possibly China, on the Security Council, and of the Arab League states as well, that may be enough to stave off the immediate threat of sanctions. But that is probably about as far as support for Syria will go. Yet another UN report released this week also condemned Syria for destabilising Lebanon by failing to staunch the flow of arms to radical Palestinian groups. Not even fellow Arab countries, such as Egypt and Saudi Arabia, have much patience left for the tiresome Mr Assad.

Economist.com WORLD AFRICA & MIDDLE EAST

Iraq

New constitution, old gripes

Oct 27th 2005 | BAGHDAD
From The Economist print edition

At last, Iraq has one—but it still may not be the final version

Get article background

IRAQ'S constitution has passed—but by the narrowest of margins, and under suspicion of fraud. As of Tuesday, October 25th, results in 14 of Iraq's 18 provinces had been announced. Those in the Shia south and in the Kurdish north had approved the constitution, with at least 95% of the electorate voting yes. The overwhelmingly Sunni Anbar province and the majority Sunni Salaheddin province however rejected the ballot with a 97% and an 82% no vote respectively. This left only one Sunni majority province—Nineveh—that could still put the no voters over the threshhold of the two-thirds majority in three provinces needed to scupper the document. When Nineveh's count was read out on Tuesday, 55% no, 45% yes, with the noes just short of the two-thirds, it was over.

Nineveh has a large Kurdish population, but even so that 45% figure looks suspicious. Saleh al-Mutlak, a prominent and outspoken Sunni politician, almost immediately declared that the elections were “faked”, and that the “Iraqi citizen knows his vote is worthless”. The country's independent elections commission declared that there was no rigging that significantly affected results. But even many non-Sunni Arabs find it easy to believe that the Kurds who live in the east of the province and who dominate its government could have padded their yes count, particularly in ethnically homogenous villages where there would be no outsiders to call foul. Some Sunni leaders have called for a fresh vote, but that is unlikely to happen.

Iraq now has a constitution supported by large majorities of two of the three main ethnic-sectarian groups, the Shia Arabs and the Kurds, but rejected by the third, the Sunni Arabs. Iraq's former ruling minority had many reasons to dislike the document's contents—the federal system split the country, they said, and allowed oil revenues to be distributed unevenly to benefit the Shia—and now they have reason to contest its legitimacy. Even before the election, some American and British officials said they were dreading this kind of result, which could stoke rather than pacify the insurgency.

However, opportunities still exist to bring the Sunnis into the political process. In a last-minute deal aimed at getting the Sunnis on board, the constitutional drafters added a mechanism to review and amend the constitution in the first half of the new year. If the turnout in the referendum is anything to go by, the Sunnis will do very well in parliamentary elections scheduled for December 15th, thus putting them in a better position to negotiate than they were this year, heavily underrepresented in parliament. Sunnis want to put forward various proposals at a national reconciliation conference sponsored by the Arab League later this year. But they will still be a minority in parliament, so it will require a genuine willingness from the other factions to make concessions to reach a consensus. And this political will has been mostly absent so far.

The adoption of the constitution and December's elections will bring an end to the succession of short-lived transitional governments that have tried to run Iraq over the past two and a half years.

Their record has been dismal. Each new minister purged his predecessor's followers, blamed failures on his predecessor, and sometimes balked at honouring reconstruction contracts signed by his predecessors. This over-swift rotation of power (together with the continuing violence of the insurgency) is blamed by many in Iraq for the creeping pace of rebuilding the country's infrastructure and has added to a general sense of the ineffectiveness of the state.

Meanwhile, the death of an army sergeant from wounds suffered in an earlier blast has pushed American deaths in action in Iraq above the 2,000-mark. About 15,000 have been wounded as well. The rate of fatalities has been remarkably consistent in the last year and a half, ever since the Americans' April 2004 attack on the insurgent stronghold of Fallujah pushed the insurgency into its current higher gear. The monthly average of fatalities has almost doubled since that battle, from 31 to about 54. Given Sunni reaction to the current constitution, there is little hope that this trend will change soon.

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Nigeria

The fat of the land

Oct 27th 2005 | LAGOS
From The Economist print edition

An anti-corruption campaign runs into politics

Get article background

AP

Alamieyeseigha: big man, big charges

IN NIGERIA, where the embezzlement of public funds is called "eating" in pidgin English, people expect to see their crooks looking well fed. To avoid the stereotype, one Nigerian state governor flew to Germany last month to have cosmetic surgery to reduce the size of his enormous belly. Unfortunately for Diepreye Alamieyeseigha, however, he was arrested on his way back through London as part of a sting co-ordinated between Nigeria's anti-corruption agency and the British police. Charged with money-laundering in Britain, he could face up to 14 years in prison if convicted.

Already this year, several other officials, including a minister, have been charged with corruption, and another state governor was arrested in London last year, though he skipped bail and returned to Nigeria. It is all part of Nigerian president Olusegun Obasanjo's much needed campaign to improve his government's reputation for tackling corruption. But, despite the high-profile arrests, doubts about the effectiveness of the anti-corruption drive abound as some question the real motivation behind the government's new-found reforming zeal.

Picking up the two state governors did not surprise anyone. Nigeria's 36 governors earn puny official salaries, but still manage to spend much of their time travelling first-class abroad. They are constitutionally immune from prosecution in Nigeria while in office, but have no diplomatic immunity. Britain, the former colonial power, is also now a keen promoter of "good governance" in Africa, and has therefore been happy to oblige in catching the two governors in its own jurisdiction. Thus encouraged, Britain was also largely instrumental in writing off $18 billion of Nigeria's external debt last week. One official in Nigeria's anti-corruption agency told *The Economist* that the agency has enough evidence to convict as many as seven more governors if they were arrested on foreign soil.

The anti-corruption campaign has helped to diminish Nigeria's reputation for corruption, but not by much. Transparency International, an anti-corruption watchdog, still placed the country sixth from bottom in this year's "corruption perception index", only a marginal improvement on the year before. It also remains true that for all the arrests, there has not been one high-level conviction during Mr Obasanjo's six years in power.

Moreover, a suspicion exists that the selection of those to be arrested might have more to do with political self-interest than any altruistic desire to purge Nigeria of corruption. Mr Alamieyeseigha may (or may not) be crooked, but he is also popular with the majority tribe in the Niger Delta, the

Ijaw, for his strident calls for an increased share of oil revenues from the central government to the delta states, including his own of Bayelsa. This angered Mr Obasanjo, who is concerned about the spreading of political opposition in the oil-rich region.

Mr Obasanjo's powerful vice-president, Atiku Abubakar, an ally of many of the governors seen as targets, also questions the direction of the anti-corruption campaign. Mr Obasanjo does not want Mr Abubakar to succeed him as president when he is constitutionally bound to step down from power in 2007. Mr Abubakar's supporters in the National Assembly had backed impeachment plans against the president in 2002 for alleged corruption—and the vice-president needs to make sure that nothing is pinned on him in return, at home or abroad. He has reason to worry. His wife's house in the United States has already been raided by police in connection with a probe against an American congressman seeking to broker telecoms deals in Africa.

The enemies of Mr Obasanjo say that his campaign against Mr Abubakar is part of his plan to amend the constitution that would allow him to stand for a third term as president. That would not enhance Nigeria's claims to democratic governance. And it could give more credence to claims that those who have done the most “eating” in these years are in fact those rather closer to the president's inner circle.

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Economist.com WORLD AFRICA & MIDDLE EAST

Eritrea and Ethiopia

Backing the favourite

Oct 27th 2005 | ASMARA
From The Economist print edition

Ethiopia defies an international ruling and its western allies do nothing

WHAT better way to settle an ugly third-world border dispute than through arbitration? What better example of conflict resolution to press upon two rancorous rivals, Ethiopia and Eritrea, who in 1998-2000 fought a bitter border war that cost 70,000 lives? That is why, as part of the peace deal that ended the war at the urging of America, the European Union and the Africa Union, the two countries asked the Permanent Court of Arbitration in The Hague to fix their border. But the court awarded the most hotly disputed piece of turf, the town of Badme, to Eritrea—the smaller nation, with a repressive little regime and few foreign friends. Ethiopia has since refused to accept the court's ruling and none of its powerful foreign allies seems inclined to try to make it change its mind.

As a result, both impoverished countries are armed to the teeth and a costly UN peacekeeping mission is hunkered along the border. And every so often come rumblings of another war, as has happened this month when Eritrea banned the UN from overflying its territory, drawing accusations from Ethiopia that it was shifting troops to the border.

The UN Security Council was due to discuss the crisis on October 27th. It fears for the safety of the 3,300 UN peacekeepers who are deployed on the border and have no mandate, or desire, to intervene in fresh fighting between two of Africa's best-organised armies. The peacekeepers are mostly on the Eritrean side, and have therefore been unable to man almost half of their 40 observation posts since their helicopters were grounded. Some observers—including John Bolton, the American ambassador to the UN—are now asking what purpose the mission serves.

It is a reasonable question: if Eritrea and Ethiopia are intent on fighting and the UN cannot stop them, the blue helmets might as well leave. Yet to blame the UN for the crisis is to miss the point. The peacekeepers were never intended to enforce peace. Rather, they were charged with deterring cross-border scuffles and reporting them when they occurred—and this they have admirably done.

Real responsibility for making Ethiopia and Eritrea honour their agreement lies, first, with their governments and, second, with those powers who urged them to accept arbitration and witnessed their agreement in Algiers in 2000. After all, western countries should have a certain influence in Ethiopia: they give it about $800m a year in development aid, a figure that could double over the next two years. Yet instead of insisting that Ethiopia accept the loss of Badme, America and the EU seem intent on having the country as their friend. For America, Ethiopia is of minor strategic importance, as an ally against Islamist extremists in southern Ethiopia and Somalia. For Britain it represents a test case of Tony Blair's ambition to fight poverty in Africa; Meles Zenawi, Ethiopia's leader, is a personal friend of Britain's prime minister, and was a member of Mr Blair's “Commission for Africa”.

Eritrea has no such posh pals. Most of the international sympathy it accrued during a bitter three-decade-long struggle for independence from Ethiopia—which it won in 1993—has since been

squandered by its despotic leader, Issaias Afwerki. Last week, an agency that monitors the world's media said that only in North Korea were journalists less free. And yet, in the dispute over Badme, Eritrea is also right; and, as its tenacious independence struggle should suggest, it is unlikely to forget it. Eritrea probably does not want another war. Its economy is still shattered by the previous one, which its conscript army lost. But its bellicose leaders are not beyond sending skirmishers across the border to make their point—and that is precisely how the last conflict began.

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Economist.com WORLD EUROPE

French protectionism

Fearful Fortress France

Oct 27th 2005 | PARIS
From The Economist print edition

French politicians could have responded to the No vote like statesmen. Instead they seek refuge behind old barriers and old ideas

FOR President Jacques Chirac, the symbolism of this week's European summit at Hampton Court was doubly awkward. His first foreign trip since going to hospital nearly two months ago, it was to the country he has most publicly quarrelled with in recent months. And the topic was how to respond to globalisation: a phenomenon which Britain faces calmly, while France remains deeply troubled.

In May, when the French voted against the Euro-constitution, they were said to be rejecting not so much the idea of Europe as what they feared Europe was becoming: a liberal, open, free-market zone. Faced with this defensive mood, two political responses were possible. Either explain that France cannot dodge globalisation; that it brings opportunity as well as pain; that the country is well-placed to adapt; and that chronic unemployment is avoidable. Or kowtow to public opinion, blame globalisation for every ill and seek refuge in old-time protectionism.

The second option was chosen. A sour protectionist mood has gripped politicians of all stripes, even those who backed the constitution. “France will never let Europe become a mere free-trade area,” wrote President Chirac in 25 European newspapers ahead of the Hampton Court meeting. His centre-right government has been incensed by the offer from Peter Mandelson, Europe's (British) trade commissioner, to cut farm tariffs as part of the Doha round of trade talks. Philippe Douste-Blazy, France's foreign minister, says Europe “must not sacrifice” the common agricultural policy (CAP): it was cut far enough by an EU deal in 2003, and Mr Mandelson shouldn't yield more.

Even would-be reformers, such as Nicolas Sarkozy, the interior minister, for whom no French taboos are sacred (especially if they are dear to his rival, Mr Chirac), has beat the protectionist drum. Mr Mandelson's proposals, he wrote in *Les Echos* newspaper, were “not acceptable”: they would bring “the dismantling of the CAP and Europe's renunciation of its status as an agricultural power”.

These outbursts follow a string of others. President Chirac bashed the European Commission for failing to stop Hewlett-Packard, an American firm, slashing its French workforce. His prime minister, Dominique de Villepin, mutters about “economic patriotism”: he denounced a rumoured takeover by PepsiCo of Danone, a French dairy firm, as an attack on a “crown jewel”, and has named ten “strategic” industries—including casinos—that must be sheltered from foreign predators.

In the opposition camp, the Socialist Party has also drifted leftwards. The policy documents offered by rival candidates ahead of the party's leadership contest in November are sprinkled with protectionist and anti-capitalist talk. François Hollande, the party's boss, calls for a “fight against economic liberalism”. Laurent Fabius, an ex-prime minister who led a breakaway faction against the constitution, decries economic liberalism as “not only unjust but inefficient”. He wants measures to protect French firms from hostile takeovers—and to penalise relocation in search of lower costs. As the government this week announced the sale of 15% of Electricité de France (EDF), the energy utility, Mr Fabius vowed to renationalise it.

Why all this protectionism? On farming, the French consensus is solid. No mainstream politician wants subsidy cuts. Mr Chirac, a former farm minister who long represented rustic Corrèze, is committed to the countryside. Farming is seen as tied up with France's regional gastronomy, its healthy food industry, plus a charming rural world that foreigners love too. A recent French cartoon showed Tony Blair basking in the garden of a French farm house. “Tony, please help the CAP,” begs Mr Chirac. “We don't care about your peasants, Jacques!” replies Mr Blair: “Agricultural land and farms will become gardens and cottages where English retirees can forget their sinister life in Britain.”

Nor is protecting farmers only a Gaullist hobby. In the 1990s, a French Socialist government's resistance to CAP reform nearly scuppered the Uruguay round of trade talks. In short, though a minuscule share of the workforce is still farming, French politicians feel compelled to turn trade-liberalisation talks into matters of national identity and well-being.

This time, France is trying not to become isolated over how much to offer the World Trade Organisation. The French say they want a successful trade round, and are not yet talking of blocking the European offer. But divisions are deep. It is possible to imagine a re-run of 1992, when French farmers held trade talks hostage.

In other areas, French protectionism is baffling. This year, while the political class has railed against globalisation, companies have been cashing in. In the first eight months of 2005, France topped the league table for European cross-border acquisitions, bagging €59.5 billion ($71.8 billion), according to Dealogic, a banking analyst. Pernod Ricard, a drinks company, bought Allied Domecq, its British rival. Suez, a utilities firm, picked up Belgium's Electrabel. France Télécom nabbed Spain's Amena, a mobile-phone operator. All this brings profits and tax revenues to France.

The paradox is not only that corporate France eagerly embraces what the politicians denounce. It is that the politicians themselves are all the while putting in place certain liberalising policies that clash with their own protectionist rhetoric. This week's decision to go ahead, albeit belatedly, with the sale of a first slice of EDF is but one example. Michel Camdessus, former IMF boss and author of a devastating critique of the French economy, told *Le Figaro* this week that “reform in our

country moves ahead in disguise. Certain measures are taken, but we are never told why." Little wonder that the electorate is confused and fearful. One poll this month showed that 80% of the French thought that the outlook was bleak, and that the social climate was bound to get worse.

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Economist.com WORLD EUROPE

Bulgarian crime

Where killing is a habit

Oct 27th 2005 | SOFIA
From The Economist print edition

Bulgaria's Euro-credibility is dented by unsolved murders

EPA

The EU dream could die too

SOME Balkan traditions, like murders in Bulgaria, die hard. On October 26th, Emil Kyulev, head of DZI-Rosexim, the country's top financial group, was shot dead as he drove to work in Sofia. The day before, the European Commission warned Bulgaria that unless it acted to curb crime in the next six months, it would not be able to join the European Union on time in January 2007.

The latest shooting was a ratcheting up of what officials in Sofia often dismiss as the “settling of accounts” by gangsters. It exacerbated the dim view taken in Brussels of Bulgaria's crime rate, and of the failure to convict any killers.

More than 50 Bulgarian mobsters have died in car-bombings and shoot-outs in Sofia and other cities in the past three years. The pace is accelerating, with eight murders in the past three months. One reason is that Bulgaria is a conduit between Turkey and Europe for trafficking in people and drugs.

A corrupt, inefficient judiciary is the biggest culprit. Police say any suspects they manage to arrest simply pay bribes to secure their release. Prosecutors and judges retort that police provide dodgy evidence. The process is snail-like; it can take nine years to get a case to court.

Sergey Stanishev, the 39-year-old Socialist prime minister whose coalition government desperately wants to meet its Euro-deadlines, admits that judicial corruption is his biggest problem. Chivvied by his cabinet, parliament finally pushed through a new criminal-procedures code, drawn up after consultations with Brussels, just hours before Olli Rehn, an EU commissioner, arrived in Sofia on October 14th. The new code meets many of his concerns. In an effort to clean house, more than 900 investigators will be demoted to pen-pushing jobs; and the pre-trial period in most cases will be cut to two months.

But it will take at least six months for the code to be implemented. New staff must be hired and trained. There is no guarantee they will be cleaner than their predecessors, or that judges will no longer be leaned on by politicians with links to the mob.

Mr Kyulev's killing differed from others in that he had apparently shaken off a shady past to become a high-flying banker and, among other things, financial adviser to the president, Georgi Parvanov. A policeman who studied business at Sofia University in the early transition years, Mr Kyulev belonged to a group of entrepreneurs who kept close to successive governments and did well in fuel and commodities trading. After surviving a banking collapse in the mid-1990s, he teamed up with Russian backers to found Rosexim bank, then bought DZI, the state insurance agency, in a privatisation deal. Unless his killer is caught and punished quickly, the European

Commission may well recommend, next spring, that Bulgaria wait another year before being admitted.

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Economist.com WORLD EUROPE

Ukraine

Sins of the fathers-in-law

Oct 27th 2005 | KIEV
From The Economist print edition

A privatisation that could mark a fresh start for Victor Yushchenko

Reuters

The white heat of a Ukrainian revolution

Get article background

THERE were no bow-tied auctioneer, and no pouting beauties bidding for phoney companies. It lasted longer than big Russian privatisation auctions tend to. But the televised sale in Kiev on October 24th had its own quirks. There was real competition, and a final price more than double the starting one. And the winner was foreign: Mittal Steel, the world's biggest steelmaker, which paid a hefty 24.2 billion hryvnas ($4.8 billion) for 93% of Kryvorizhstal, Ukraine's biggest steel mill.

Before and during the “orange revolution” that brought him to power, President Victor Yushchenko made Kryvorizhstal a totem of the corruption that prevailed under Leonid Kuchma, his predecessor. The mill had been flogged for just under $800m, shortly before last year's presidential election, to a consortium that included Victor Pinchuk, Mr Kuchma's son-in-law. The courts returned the stake to the state in June. Mr Yushchenko hailed the resale as proof that his country was capable of staging honest privatisations.

More than that, the event had become a test of the president's ability to get anything done. His first government was crippled by personal and financial rivalries. In September, amid an orgy of corruption allegations, he fired Yulia Timoshenko, the formidable demagogue he had appointed as prime minister, and lots of other people. Since then, the intra-government rifts have migrated to an already-fractious Rada, Ukraine's parliament. With typical patriotic zeal, the Rada last week passed several resolutions aimed at stalling the steel auction. Oleg Rybachuk, Mr Yushchenko's new, straight-talking and (it seems) clean chief of staff, says the government feared that communists, socialists and oligarch fellow-travellers would disrupt the event.

In the end, the few protesters only booed and flew communist flags. And despite these efforts, the sale price exceeded expectations, though the Mittal men seem pleased too. Attending in an uncertain capacity, Mrs Timoshenko made sure she was first to congratulate them. “It was like a football game,” she gushed.

The most palpable result is the $4.8 billion. Though tax and customs receipts have risen, Mrs Timoshenko's rash policies contributed to a slowdown in growth. Stretched by the cost of electoral promises, the government needs the Mittal cash, which is more than all Ukraine's previous privatisations put together have raised.

Will this be a turning-point for Mr Yushchenko? Probably not. The “re-privatisation” of enterprises sold off under Mr Kuchma—part of a broader question over how to address past injustices—was the hottest issue for the short-lived Timoshenko government. It was her aggressive bid to take back a big ferro-alloy plant (controlled by, er, Mr Pinchuk) that sealed her fate. The new sale didn't resolve that dilemma; it may have worsened it.

Mr Rybachuk says that from now on the “basic principle” in addressing controversial deals will be “amicable agreement” with the current owners. But there is as yet no clear policy, and the case for taking back and reselling companies might now look stronger. Unfortunately, with this parliament and these oligarchs, that would be perilous.

Parliament is itself Mr Yushchenko's biggest problem. Even before he sacked Mrs Timoshenko, he struggled to control the Rada: witness the palaver over the laws needed for Ukraine to join the World Trade Organisation. Conventional wisdom says life will get easier for him after the parliamentary election due next March; some presidential powers are set to pass to the Rada and a new prime minister.

Conventional, but optimistic. Current polls show roughly equal numbers for Mrs Timoshenko's block, Mr Yushchenko's supporters and the party led by Victor Yanukovich, his opponent in the presidential vote. Predictions are risky in Ukrainian politics, but it seems Mr Yushchenko's team will be obliged to choose between two unpalatable options. One is a rapprochement with Mrs Timoshenko, who would almost certainly want her old job back. The other would be a parliamentary coalition with Mr Yanukovich, with whom the president was obliged to cut a mini-deal to secure the appointment of an interim prime minister. “Pragmatic compromise”, says Olexiy Haran, a political analyst, “is part of Ukrainian politics;” but for many who stood in the snow last year to keep Mr Yanukovich out, that would be a compromise too far. It would also slow Ukraine's limping westward integration.

It isn't all bad. The country has freer media than under Mr Kuchma, and a more assertive citizenry. It has seen a government sacked over corruption (which is better than a corrupt government that isn't sacked), and got $4.8 billion for a steel mill. But the steely-nerved protesters who led the orange revolution deserved more.

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Economist.com WORLD EUROPE

Turkey

Caught between two worlds

Oct 27th 2005 | ANKARA AND ISTANBUL
From The Economist print edition

A small victory for gay Turks

THERE was a sense of déjà vu last month when the Ankara governor's office told prosecutors to ban KAOS-GL, a gay-rights association, for promoting “immoral” activity. After the prosecution of Turkey's famous novelist, Orhan Pamuk, liberals saw the news as yet another sign of reactionaries at large. In fact, the anti-gay move probably began not with homophobic bureaucrats, but with ultra-nationalists sabotaging Turkey's ties with the European Union.

They failed. Talks with the EU began as planned on October 3rd. Ten days later, it was announced that no charges would be filed against the gay group. Citing the European Convention on Human Rights, a prosecutor, Kursat Kayral, said that being homosexual did not mean a person was immoral. “Those who study morality”, he added, “would all agree that the most precious right for human beings is the right to exercise their free will.” This was the first time officialdom had ruled in favour of gay rights: new ground not only for Turkey, but for the Muslim world.

“We are delighted,” said Ali Erol, a founder of KAOS-GL. Set up in 1994 as a support group for gays and lesbians, it was only in July that KAOS-GL sought recognition as an association. Why so long? Mr Erol's reply sums up the problem faced by gays and other minorities in Turkey. “As long as we did not publicly assert our identity, or seek protection of rights, we were left alone. When we sought legitimacy, they tried shutting us down.”

Many gay Turks agree that despite the social pressures they face, their lot is not bad compared with that of gays in other Muslim countries where penalties range from jail to death. No Turkish law bans same-sex relations. This tolerance dates back to the Ottoman era when sultans would bring winsome boys on military campaigns. A gay culture, captured in miniatures and poetry, flourished in public baths and the harem.

In the 19th century, as Turkey began aping the West, attitudes hardened. After the founding of the modern republic, in 1923, the state insisted more strongly on conventional family life. When the army took over in 1980, it crushed “deviance”: transvestites were jailed, and a trans-sexual singer, Bulent Ersoy, tried to kill herself after failing to be recognised as a woman.

Today Ms Ersoy carries a pink identity card issued to women. Gay clubs have mushroomed in cities like Ankara, Izmir and Istanbul, where your correspondent spotted a transvestite wearing an Islamic headscarf. Cross-dressing show hosts are a staple of Turkish TV. Meanwhile, thanks to the internet, gays in the conservative east can make contacts in the liberal west.

But gay life is largely hidden, especially in the workplace, where homosexuals fear for their jobs. Groups want changes to the penal code, banning discrimination on the ground of sexual preference. They cite the army, where homosexuality is seen as a “psychological disease”—and officers found “guilty” are disgraced and court-martialled.

For the mild Islamists now in power, gay rights could be a sticking-point in relations with the EU.

With Islam deeply opposed to homosexuality, can they risk alienating conservative voters and pass pro-gay legislation? “Absolutely not,” said a spokesman for the ruling Justice and Development Party. “We will never endorse an openly homosexual candidate.”

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Poland's election

Twins together, Poles apart

Oct 27th 2005
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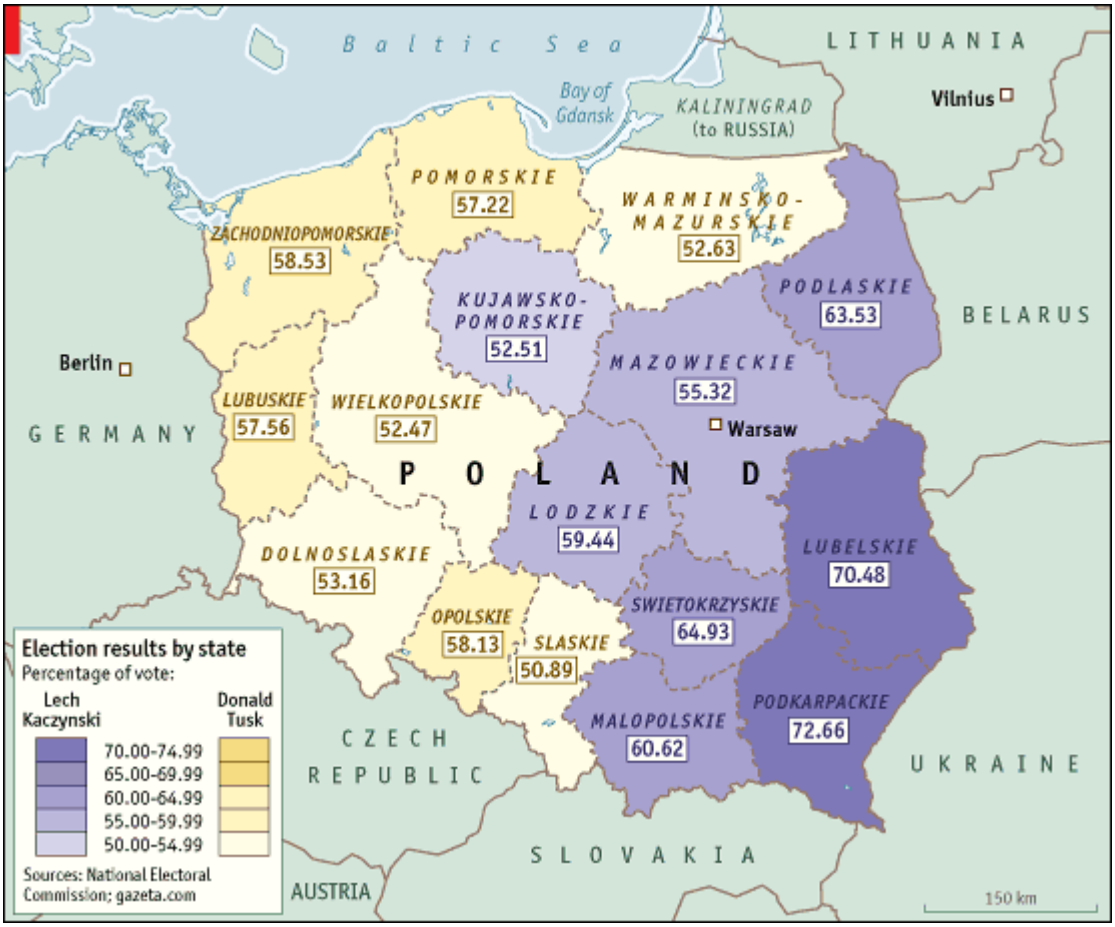

The electoral triumph of two tub-thumping brothers raises questions about Poland's enthusiasm for change

Get article background

IF POLAND'S presidential election had gone as expected—with victory for a dull, worthy economic reformer—then the rest of Europe would hardly have looked up. Instead, the European Union's biggest newcomer gave its partners a rude shock, and laid bare some deep worries about the pace of social and economic change.

Even among Poles who rejoice over the end of communism, and therefore identify with the centre-right, there are still huge differences—and the traditionalist camp, with old ideas about the family, the farm and foreigners, is stronger than anybody thought. That, broadly, was the message delivered on October 23rd by the Polish electorate when it gave a 54% score to Lech Kaczynski of

the Law and Justice (PiS) party, against 46% for his rival, Donald Tusk, from the pro-business Civic Platform (PO). Following a general election last month, in which the conservative parties trounced the left, the result snarled up a coalition building effort, under way since. Instead of a broad centre-right coalition, Poland faced the possibility of a minority government led by PiS and drawing support from the ultra-populist right.

On October 26th, relations between PO and PiS fell to a new low when, at the latter's behest, a zealously Catholic and Eurosceptic politician, Marek Jurek, was installed as speaker of parliament. PiS initially suggested that this post could go to a moderate figure, nominated by PO, but negotiations over top jobs apparently broke down. Bargaining continued, but from Civic Platform's viewpoint, it might be better to allow its rivals to form a fragile minority government, rather than share responsibility for a coalition over which it has little influence.

For the president-elect, Lech, and his twin brother Jaroslaw, the chairman of PiS, the presidential result capped an astonishing run of political success. The tub-thumping pair, who won national fame in 1962 as child film stars with sweet faces, have apparently found a winning formula in social conservatism, religious nostalgia and promises to assert Poland's interests. As mayor of Warsaw, Lech Kaczynski has barred gay parades, backed the death penalty and resisted pressure to adopt a more cosmopolitan style.

His brother, who might in theory have become prime minister after the general election last month, has nominated a modest teacher-turned-economist, Kazimierz Marcinkiewicz, for that job instead. But in Poland's political castle, Lech and Jaroslaw, who were born 56 years ago to a famous resistance fighter, have been left as king and king-maker respectively.

President Jacques Chirac of France was among the first European leaders to congratulate King Lech, and immediately invited him to Paris. That might be a telling sign. Instead of showing the world a reformist, centre-right face—in tune with Germany's chancellor-to-be, Angela Merkel—politics in Warsaw may be taking on a more Gaullist hue: nationalist and wedded to farm interests, with a dose of Polish clericalism thrown in. And among federally minded Eurocrats, the election result was greeted with muffled groans. Some took offence at the new president's dismissal of Brussels as “a city in which some kind of subsidies are agreed upon”.

Meanwhile, Poland's liberal, pro-European establishment was left wondering how it miscalculated the strength of traditionalist sentiment. Did people underestimate the fear of externally imposed change in a nation where outsiders have usually arrived as invaders?

It depends, of course, on which part of the nation you mean. It is hardly news that Poland's east and south-east—much of which used to be part of Russia—are poor and conservative, while the north and west—formerly part of Germany—are more liberal and open to change. In the ex-Russian regions, Catholicism was a badge of identity which marked Poles out from the Orthodox neighbours; people cling to it all the more fiercely. Those areas have an Orthodox minority, also conservative.

In the latest election, voting patterns followed the dictates of history and geography more closely than ever and in ways that were not always obvious. Most of the families who now live in the ex-German territories originate from the east, and only moved west after borders were redrawn in 1945. But that does not make them conservative now: life in formerly German lands, where the infrastructure is good and contact with westerners frequent, has made people more open to change. Nor is the east all conservative: in deep-blue places like Podlaskie, there are places where Mr Tusk did quite well—rich tourist areas.

If prosperity gives people “modern” views and voting habits, then liberals should be taking comfort. And people like Janina Paradowska, a political analyst, see crumbs of reassurance. “A

large part of the population voted for a liberal vision of Poland. Where else would you see a party [like PO] with such a liberal economic agenda getting such wide support?"

Wide, but apparently not wide enough. Some Poles had hoped they might finally get a government dominated neither by cynical ex-communists, nor by moralising anti-communists fixated on the past. They may have to wait a while longer.

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Charlemagne

Europe's Cassandra complex

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Like those ancient songsters, the European Union can warn and lament—but not act

EARLY on, there were 12 members. Later, 15. In subsequent versions, you can see 25, perhaps more. No, not growth in membership of the European Union. This is also the history of the number of people in the chorus of classical Greek drama.

How apt. In foreign policy, says Bob Kagan, of the Carnegie Endowment think-tank, the EU is just like a Greek chorus. It comments on the action. It reacts with horror or praise. It interacts in various ways with the protagonists. But the singers themselves play no part in the plot.

“O horror!” Europeans might reply, “Horror recoiling a thousand times! We may be old but our country's strength is young and lusty still” (“Oedipus at Colonus”). In simpler terms, the Europeans still yearn to go beyond what they have achieved at home (peace on the continent) and in their neighbourhood (modernising Turkey and pacifying the Balkans with the lure of membership). As it looks farther afield, the Union can already take pride in some peacekeeping missions in distant places, like Indonesia. European countries play a leading role in anti-nuclear diplomacy in Iran. European troops are in Afghanistan. The EU spends considerable sums in Palestine.

But whether this adds up to a coherent global policy is doubtful. Even if it does, the EU does not really formulate or carry out that policy (the troops in Afghanistan are NATO's; the Iranian diplomacy is pursued by Britain, France and Germany). But the EU is the main forum for its members to comment on and react to world events. So it is, at least, a chorus, not a cacophony.

The Greek chorus represented the community. It voiced the reaction of ordinary folk to the (often

horrible) events in their midst. The EU also sees itself as a benign observer: no less keen on universal ideals (democracy, liberty) than America, and more sensitive than America to things like development and poverty.

As in the EU, the chorus often expresses support for the “law”. In Sophocles's “Antigone”, the chorus chides the heroine for “stumbling against Law enthroned”—a bit like EU members complaining of America's cavalier attitude to international norms.

The Greek chorus has a privileged relationship with the protagonists: its leader often stops in mid-commentary to talk to the hero and praise or upbraid him for his intended actions. As the part of the world that shares a vision of democracy and human rights with America, Europe should, in theory, be well-placed to advise and warn America about its policies. The EU already plays a moderately useful role in going through the diplomatic motions—in Iran and the Middle East, for example—when America does not know how, or whether, to get involved.

On the other hand, the Greek chorus is frequently made up of doddery old men—Theban elders in Sophocles's “King Oedipus” and “Antigone”; old justices in Aristophanes's “The Wasps”. Or it is made up of women (Euripides's “Medea”). Either group, in the Greek world, was out of the decision-making loop—as the Europeans frequently are in Washington.

Sometimes, the chorus has no clue what is going on. “I am at a loss for thought,” says the leader of the chorus of mothers in Euripides's “Suppliants”. “I have no idea where to turn.” Frequently, it is terrified, as at the start of “King Oedipus” (“my spirit is riven with fear of what will happen”). And sometimes, the members of the chorus are figures of derision, as in the “violent, old, splenetic men” of “The Wasps”. The chorus almost always splits into different bits—not an unknown feature of the EU, where there are three centres of foreign policy-making: the European Commission, the Council of Ministers and national capitals themselves. Doddery, clueless, fearful and divided—it could be Donald Rumsfeld talking about old Europe.

It is fair to say that, ten years ago, the EU had no real foreign-policy involvement, except in trade. Now it has missions all over the world; troops in a few hotspots; and its individual members are somewhat more wary of going out on a limb than they used to be (though of course they still act unilaterally when they really want). It has a preference for soft power, and mild assertions of influence. What it does not have is an active and coherent global policy—because its members do not want it to.

Singing from the sidelines

The result, in EU policymaking and Greek drama, is inconsistency and ineffectiveness. In “Agamemnon” and “Antigone”, those in power take big, atrocious decisions: Clytemnestra to murder the king; Creon to punish an enemy to excess. The chorus knows the protagonists are giving way to hubris, which will lead to disaster. It even tries to warn them, but no one pays any notice. In Agamemnon, the chorus flees in a panic when Cassandra prophesies the king will be killed. And while the murder is taking place, the chorus is reduced to nattering and yammering. “This is what I say, send a herald round.” “Too slow. I say we should burst in at once.” “I can suggest no plan that might prove practical.” “I agree with you.” It all sounds a bit like the EU before the Iraq war.

Elaine Fantham, a professor emerita at Princeton University, points out that the Greek chorus is governed by three basic rules. It may talk to the protagonists but cannot do much with the information it receives (such as pass it on to others); it does not necessarily understand what is really going on; and it cannot affect the main action, no matter what it says or knows. Something similar might be said about the EU. It plays a part in international diplomacy. But it does not have

a true global policy. And as a result, it has little influence over those that do.

Of course, there is another aspect to this analogy. If the EU is the chorus, America must be the protagonist or tragic hero, hurrying to his doom and reckless of the consequences of his actions. In Aeschylus's “Persians”, the over-reaching Xerxes mounts a hubristic expedition to punish Athens and is defeated and humiliated. But that's another story.

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Economist.com WORLD EUROPE

Politics and class

The not-so-common touch

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Why being posh now matters less than it used to in British politics

ONE of the few things people can agree on about Britain's class system is that it is always out of date. “The peculiarity of English class distinctions is not that they are unjust—for after all, wealth and poverty exist side by side in almost all countries—but that they are anachronistic,” George Orwell wrote back in 1947. More recently, Andrew (now Lord) Adonis, one of the brains behind this week's education white paper, helped write a book arguing much the same. Old ideas about monocles and stately homes were misleading. These days Britain's elite was made up of a super-class that married inherited wealth with brains. In the absence of any reliable way to identify people as upper-class, though, one indicator has persisted: where they went to school.

Both Tony Blair and David Cameron, who is now the favourite to be the next Conservative leader, went to top private schools, and so on this measure are members of a small elite. In fact their educational backgrounds (both went to Oxford too) are even closer than this suggests: Mr Blair's housemaster at Fettes, Eric Anderson, went on to be Mr Cameron's headmaster at Eton.

An adolescence spent at an expensive school with archaic rules and an absurd dress code was until recently thought to be a handicap for a politician. Though the Conservative Party has always selected more than half of its MPs from among the privately educated, the party has not been led by someone who went to a private school since it picked Alec Douglas-Home in 1963. Yet last week a poll by MORI found that 74% thought Mr Cameron's formative years in a tailcoat and a starched collar would not count against him. Only 15% reckoned his schooling was a handicap. As a result, Mr Cameron has been able to insist that “it's not where you come from but where you're going that counts.” In the class-ridden world of British politics, that counts as a novel idea. What changed?

Mr Cameron's youth undoubtedly helps—it's harder to sound patrician when you're only 39. But three changes have also smoothed his ascent. First, New Labour has made life a little safer for upper-crust Tories. Though Labour has had privately educated leaders before (Hugh Gaitskell, Clement Attlee and Michael Foot all went to embarrassingly smart schools), Tony Blair is the first to have used his private education as a way of reassuring upwardly mobile middle-class voters, who backed Labour for the first time in 1997, that his party really had changed. Attacking a Conservative for being privileged would risk putting them off. It might also sound hypocritical: nine out of the 23 members of Mr Blair's cabinet, including the education secretary, Ruth Kelly, and her predecessor in the job, Charles Clarke, attended private schools at some stage.

Second, British politics has become less tribal and more managerial. Arguments over education this week provide a good example, with the government arguing that it has found a new way to improve state education—making schools more independent of the government—and the opposition replying that they thought of this first (see article). When policy divides are no longer founded on class ideologies, the backgrounds of those arguing over them matter less.

Third, the Conservative Party has changed, too. In the 1980s the party discovered economics and

positioned itself on the side of the honest, hard-working opponents of entrenched interests—including the privileged. The change in attitude was reflected in the people who got the top government jobs. Of the 22 members of Margaret Thatcher's cabinet in May 1979, 20 were privately educated. By 1990, John Major's cabinet was less posh and the ratio was down to 14 out of 22. Now there is an even split in the shadow cabinet between those educated at the expense of the taxpayer and those whose parents paid the bills. But even as they became the party of creative destruction, the Conservatives lost the knack of sounding likeable and even ceded aspiration to Labour. Paradoxically, many of them now think that privileged Mr Cameron can restore both.

In both main parties, the leader's background now matters less than his powers of communication. Gordon Brown has a more compelling personal story than Mr Blair does: he was born into a humble family and rose fast by being exceptionally clever and hardworking. But this on its own counts for little set against the natural charm that Mr Blair has used to such effect. Far from assuming that Mr Brown's background alone will convince voters that he understands their concerns, Labour strategists worry about how he will look and sound on breakfast television.

Likewise in the Conservative Party, David Davis (who is challenging Mr Cameron for the party leadership) has what politicos call a great backstory. He was brought up on a council estate by a single mother, went to an ordinary school and became a successful businessman. Yet according to opinion polls, most Tory members think posh Mr Cameron would do a better job than Mr Davis of appealing to voters who tell pollsters that the Tories do not share their values.

That does not mean that either Mr Blair or Mr Cameron is free to look and sound like members of the gentry, though. Mr Blair's accent (another reliable class marker) used to wander around the country according to who was in the audience, with flecks of estuary English creeping in for some and the Oxford variety returning for others. By speaking in short, verbless sentences that are a long way from the rolling oratory of the Bar, where he learned to speak in public, Mr Blair has now developed a way to sound classless.

Mr Cameron's background as an Etonian son of a stockbroker who married a baronet's daughter is harder to shake off than Mr Blair's. But he, too, has portrayed himself as an ordinary man who just happened to have a privileged upbringing. Cartoonists have drawn him as the “Blue Boy,” an 18th-century painting by Gainsborough of a young aristocrat in a lacy collar, and also as a country squire, striding around in tweed. Mr Cameron has responded by telling people that he drives a cheap car and prefers beer to champagne.

All of which might sound disingenuous, if many members of Britain's middle class were not engaged in a similar game of downplaying their good fortune. In the past 40 years, Britain's middle class has expanded while its working class has shrunk, as manual labour became scarce and more people found work behind a desk. But, a separate MORI poll found that 55% of middle-class Brits call themselves working-class. Both Mr Blair and Mr Cameron are therefore perfectly representative of a large and influential part of British society that is successful, well-to-do and just a little embarrassed about it.

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Oxbridge

Dons go a-begging

Oct 27th 2005
From The Economist print edition

Oxford and Cambridge both want to be given lots more money

Get article background

PICTURE an Oxbridge don and you probably imagine a gown-wearing eccentric, sipping port in ancient panelled rooms that look out on to some of Britain's most beautiful views. It is hardly an image that conveys the impression of poverty.

Yet both Oxford and Cambridge say they need more money, and lots of it. Last month Cambridge launched its 800th Anniversary campaign, which aims to raise £1 billion ($1.8 billion) by 2012. A reception for selected alumni and VIPs was held in London on 27th October, with similar events to follow in San Francisco, New York and Hong Kong. On 1st November Oxford's vice-chancellor, John Hood, will put new governance proposals before Congregation—the dons' parliament with ultimate authority in the university—in the hope of making Oxford more attractive to donors. His earlier attempt to simplify the university's arcane decision-making was rebuffed by Congregation in May, after a poisonous row over whether it would destroy Oxford's unique character.

The argument of traditionalists has been that for most of its history Oxford has had only one competitor—Cambridge (known archly by many as “the other place”). Hence it must be doing something right. But both Mr Hood and Professor Alison Richard, Cambridge's Vice-Chancellor, are focused on what they regard as the real competition: Harvard, Yale and Princeton. Although Cambridge and Oxford ranked third and fourth in a listing of world universities published this week by the *Times Higher Education Supplement,* the vice-chancellors are worried by what they see. Their American rivals have far larger endowments. Yale, where Ms Richard was Provost until recently, has an endowment pushing $13 billion, around three times the size of Cambridge's, and Harvard is even richer.

The public sees Oxbridge primarily through the eyes of students, but students don't see much of what happens in a university. Their lives centre around colleges and lecture theatres, not the departmental offices and laboratories where academics do what they consider their real work.

Real life for many Oxbridge academics is much less rosy than the fantasy. Quite a few are on short-term contracts and don't belong to a college at all. Even for those that do, the luxury often ends abruptly at their college gates. Many departments became horribly run-down during the funding squeeze of the past few decades. Until recently, Cambridge mathematicians who hold professorial chairs as eminent as the one occupied by Isaac Newton (with college rooms to match) had to slum it in a department that resembled nothing so much as a shabby rabbit warren.

Cambridge maths has recently moved to a smart new £60m Centre for Mathematical Sciences, more than half of which was paid for by donations. The centre is only one of several fancy new university buildings: over the past seven years, Cambridge's “footprint” has increased by 20%. Students benefit too, because the university's prestige and the value of its degrees ultimately depend on the quality of its academic research. Star academics can't be recruited and kept by

picturesque colleges alone; they want excellent departmental and laboratory facilities, top-flight collaborators—and money.

Some of this can come from previous students. “We need to educate our alumni about what we do,” says Ms Richard. She says the fund-raising campaign aims to establish new habits of giving, and to develop a group of alumni who can act as “ambassadors” for the university's work.

But to build the new facilities they need, the two universities must woo large donors, too. Such people want to see convincingly costed plans, and tend to be unimpressed by the anti-business rhetoric which academics sometimes indulge in. Often they expect something in return for their cash, such as having a building named after them (Cambridge's maths centre has the Faulkes Institute of Geometry and the Betty and Gordon Moore Library), and to negotiate with someone with the authority to make this happen.

Making Oxbridge attractive to donors will create losers, however. Rich alumni may end up funding laboratories for their old departments, rather than libraries for their old colleges. College heads might be resigned to that—many are, after all, distinguished academics with strong departmental loyalties. But it may be harder to persuade some college fellows passing the port in hall to be as high-minded.

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Environmentalism

Virtue for sale

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How to persuade people to go green

LAST month British Airways (BA) announced it would give passengers the chance to do their bit for the planet by letting them pay a few pounds extra on every ticket and use the money to offset the carbon emissions from their trip. Last week the airline admitted that, so far, hardly anybody seems interested, with fewer than 1 in 200 passengers willing to cough up. That sits oddly with people's professed anxiety in polls about climate change.

BA points out that the scheme is new. Greens accuse it of failing to do enough advertising. Economists spy an example of what they call revealed preferences—the idea that talk is cheap and actions provide the best guide to somebody's beliefs. The cost of cutting carbon emissions is immediate but benefits are deferred and thinly spread. Appeals to people's better natures tend to fall flat if they involve demands on their wallets.

So, too, in electricity, where some firms offer “green tariffs”, which typically charge more for carbon-free renewable energy. Many greens are disappointed with the take-up of such schemes. Companies guard such information closely, but *The Economist's* calculations suggest one company, EDF Energy, has signed up only around 10,000 homes in London and the South East (out of several million eligible customers). Npower, another energy firm, offers, in partnership with Greenpeace, a tariff at the same price as its other contracts. Its scheme is full, because consumers pay no premium, says Greenpeace's Stephen Tindale.

But it doesn't take much self-interest to trump tight-fistedness. Organic food costs more and confers no scientifically proven benefit on those who eat it. But, in the land of BSE, people doubt scientists and sales are soaring among those who would rather not take chances. BA itself illustrates the point: whatever the airline's green scheme does for the planet, it has done BA's brand no harm.

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The BBC

Bush House of Arabia

Oct 27th 2005
From The Economist print edition

The BBC takes on al-Jazeera

Get article background

PEOPLE in the Middle East, it seems, are longing for BBC television news. This week the BBC's World Service announced that it will launch a new Arabic television channel in 2007. As evidence of strong popular demand, it quoted a survey of seven cities in the region which found that 85% of people would be likely to watch such a service. The World Service is also catering to political demand. Diplomats in Britain and America want something moderate to counter the influence of al-Jazeera, a controversial satellite-television station which shows civilian deaths in Iraq and videotapes from Osama bin Laden.

To the same end, America started an Arabic-language satellite-television service called al-Hurra in February last year. It is not popular. The BBC expects its service to have more credibility, since it has been broadcasting an Arabic radio service since 1938. Viewers in the Middle East will also remember how the BBC got into trouble after one of its reporters accused the British government of exaggerating the case for war against Iraq.

The new service will cost £19m ($34m) a year. The Foreign Office, which funds the World Service, refused to provide any extra money, so the World Service will have to make cuts in other services. From March next year, there will be no more radio broadcasts in Bulgarian, Croatian, Czech, Greek, Hungarian, Kazakh, Polish, Slovak, Slovene or Thai.

These days, certainly, young Arabs are more inclined to watch satellite TV than tune in to BBC radio as their parents did. But some people argue that the BBC is too late into TV, because there are already several channels expressing various points of view. Not that long ago, viewers had little beside heavily censored state-owned channels. But the launch of al-Jazeera from Qatar in 1996 prompted the birth of other, freer, local channels, such as Saudi-backed al-Arabiya, out of Dubai, and Abu Dhabi TV. The BBC does have credibility with Arab audiences, says Jihad Ballout, a spokesman for al-Arabiya, “but there are now better sources about our region”.

The Foreign Office's money would have been more effectively spent back in 1994-96, when the BBC had an Arabic-language satellite-television service up and running with financial backing from a Saudi-backed company called Orbit. The station went off the air in 1996 because the Saudi government objected to the BBC's programming—in one instance, to a news item about King Fahd being admitted to hospital. No other funding was available then, and the Arab-speaking television journalists trained by the BBC went off to start al-Jazeera.

The BBC's new channel will be based in London, with several bureaus in the Middle East. It will air a mix of news, information, discussion programmes and debates for 12 hours a day. The hardest task will be coming up with programming that its rivals do not already have a version of. A suggestion, from an editor at al-Arabiya, is that Arab satellite television mostly concentrates on hard, breaking news stories. There is a big gap, he says, for smaller, personal stories about

people's daily lives.

Just as the BBC builds its new service, al-Jazeera is preparing to launch its own English-language service next spring. Two of its most high-profile recruits are Josh Rushing, a former Marine who first encountered al-Jazeera as a spokesman for the American army in Qatar, and David Frost, until May a presenter for the BBC.

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Worker relations

Time to talk

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New laws on workplace representation are a waste of everyone's time

IN MANAGEMENT, the girl-band Bananarama might have sung, it's what you do, not the way that you do it. Sadly, the thought is lost on those in Europe who proposed rules that have since April allowed British workers to group together and demand information on subjects such as corporate strategy and hiring and firing. A survey published this week by IRS *Employment Review*, a journal, concluded that two-thirds of firms now have some kind of works committee; a quarter have set one up in the past two years. Today, the rules apply to firms with more than 150 workers; by April 2008, any firm with 50 will have to comply.

The rules' main backers are the trade unions. Historically, unions have been against such laws, fearing that they would be company-controlled and would therefore undermine their power. But modern unions have been losing private-sector members for decades, and there is now little power to preserve. Their support is pragmatic, not ideological. “We're not opposed, because of the change in the industrial relations landscape,” says Sarah Veale of the Trades Union Congress. “This is another opportunity to represent workers.”

Business groups doubt the laws are needed. Small business is unworried about their impact. “Even when the limit drops to 50, this will still miss 90% of the firms in Britain,” says Stephen Alambritis of the Federation of Small Businesses. Richard Wilson, the head of business policy at the Institute of Directors, worries that they will make management too formalistic, and points out that it always was in a firm's interest to keep its staff well-informed. Many big companies already have such schemes, and those that do not may be tempted simply to formalise a few procedures and carry on as before.

Where communication is a problem, the real issues lie elsewhere. According to a survey of workers published last month by CHA, a consultancy , the main grouse is the quality of the information and how it is presented. Two-thirds of workers think they get too much irrelevant guff from management, and most prefer the boss to talk to his underlings in person rather than publish his thoughts in an obscure corner of the company intranet.

The law is too blunt an instrument to fix such things. Indeed, the law need not get involved at all: commercial forces are a more potent incentive for managers to improve their people skills. CHA's research shows that people who feel they are being kept in the dark tend to vote with their feet. “I find it hard to believe that this is a pressing issue,” says Mr Wilson.

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Music industry

Monkey business

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Matt Writtle

Music charts began as a way for record labels to market their acts. How galling then for the industry that the number-one spot in this week's chart was taken by Arctic Monkeys, a band from Sheffield whose first professional single owes its existence not to the image-makers but to internet file-sharing. The band began by handing out free CDs with rough versions of songs at concerts. Songs were made available on the band's website and e-mailed between fans. Now, says Johnny Bradshaw of Domino (the label that belatedly signed the band), when Arctic Monkeys play concerts, 1,500 people sing along to songs that have not yet been released. Even more sweetly, the band seized the top spot from the Sugababes, a manufactured pop act with sculpted eyebrows and perfect hair. Though bands have used the internet to market themselves before, none has won such commercial success without the help of a record company. “If I were a major record label, I'd be firing my A&R man,” says Mr Bradshaw. There is some comfort for the industry as it contemplates the threat to its revenues from the internet, though: at least enough fans went and bought the single to send it to number one.

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Takeover of Marconi

Business past, business future

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The pension-fund hole determined the terms of the deal

AT THE height of dotcom madness in 2000, it was a company worth £35 billion. Before then, as GEC, it had been one of Britain's top manufacturers, run by the redoubtable industrialist, Arnold Weinstock. But on October 25th, the bulk of Marconi was bought by Ericsson, a Swedish telecommunications group, for a piffling £1.2 billion.

The sale closes an ignominious episode in British commercial history. All that remains of the industrial giant that Lord Weinstock assembled is a small telecoms-services company. Called, uninspiringly, telent—Ericsson has purchased the Marconi brand—it had sales of only £336m in the last financial year.

But the deal casts light on Britain's business future, as well as its past. These days the state of company pension funds can decide the fate of takeover bids. The role of the Pensions Regulator, chaired by David Norgrove, in clearing takeovers has become a pivotal one.

Telent may now have only 2,100 employees, but it remains responsible for the Marconi pension scheme, which has 69,000 members, of whom 38,000 are pensioners. The total liabilities of the scheme are estimated under the FRS17 accounting standard at £2.5 billion. The pension fund's assets come close to that, leaving a deficit of £109m.

However, the regulator has insisted that more than half the purchase price must be used to safeguard the interests of the pension-scheme members. Of the £1.2 billion that Ericsson is stumping up, telent must set aside £675m to prop up the pension fund. Of this sum, £185m will be injected into the fund and £490m will be put into a special secure account to cover any future shortfalls.

The regulator's prominent role arises from new powers to ensure that mergers and acquisitions take into account the interests of the pension scheme. Mr Norgrove wants to reduce potential claims on the Pension Protection Fund, which now provides a safety-net for members of underfunded pension schemes whose employers go bust. He has highlighted the fact that a pension-fund deficit is in effect an unsecured loan to the company.

The regulator wanted to secure as much money as possible for the Marconi pension fund not just to plug today's hole, but also to provide for possible future shortfalls resulting from adverse market movements. A big company could cope with these. The worry is that given the size of the

Marconi fund, they might be beyond the capacity of telent, with an expected market capitalisation of only £200m, to make good.

The salience of the pension scheme in determining the terms of the Marconi sale outlines the shape of deals to come. For any merger or acquisition involving firms whose pension funds are in deficit—and there are plenty of them around—the first port of call will be Mr Norgrove's office.

The Marconi deal could also generate a new business market for mature occupational pension schemes. Understandably, telent wants to be something more than a small company attached to a huge pension fund. It will seek to dispose of the pension assets and liabilities to a financial institution, such as a life-insurance company. There might also be potential interest from companies like Resolution that have grown rapidly in recent years by swallowing up closed life-insurance funds.

Lord Weinstock himself built up GEC through a succession of pioneering takeovers. Now Marconi is being sold in what looks set to be another pathfinding deal.

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Libel costs

Naomi's chilling effect

Oct 27th 2005
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The law lords question "no win, no fee" agreements in libel cases

PA

High-cost Campbell

LAST year, the House of Lords, Britain's highest court of appeal, decided Naomi Campbell was entitled to £3,500 damages for a violation of her privacy by the Mirror Group Newspapers after it published details of her treatment for a drug addiction. Now the court has ruled that the group must also pay the model's legal costs, totalling more than £1m under a "no win, no fee" agreement. Such an agreement was compatible with the group's right to freedom of expression, they concluded.

The ruling will add to the growing unease among the judiciary as well as publishers over what Lord Hoffmann, one of the judges in the Campbell case, described as the potential "blackmailing effect" of conditional fee agreements (CFAs). Under these, a claimant in a civil action may agree with his lawyers to pay them up to double their normal fees if he wins and nothing if he loses. Introduced for libel suits in 1999, CFAs were supposed to ensure that such claims were no longer just a rich man's preserve. But, often involving costs out of all proportion to the actual damages awarded, they are increasingly seen as a serious threat to the press's ability to publish information which it is in the public interest to expose.

This applied in particular where impecunious claimants do not take out "after-the-event" legal insurance with which to pay the other side's costs if they lose, Lord Hoffmann suggested. While enabling people of modest means to protect their reputations, the CFA system could also encourage frivolous claims, tempting the claimant to press on with a hopeless case at no risk to himself.

He cited a recent libel action brought against the owners of the *News of the World* by Bogdan Maris, a failed Romanian asylum-seeker and petty criminal, acting under the false name of Alin Turcu. Claiming that the paper had defamed him by linking him to an alleged plot by an

“international terror gang” to kidnap Victoria Beckham and her two children, Mr Maris sued the paper for huge damages. His claim, brought under a CFA, was thrown out and costs awarded against him. But, bereft of both funds and insurance, Mr Maris was unable to pay.

In such circumstances, Lord Hoffmann said, media defendants must be tempted to settle out of court, however strong their case, so as to avoid litigation involving potential liability not only for the defendant's normal legal fees, but double that if they lost, and no reimbursement of their own costs if they won. “The obvious unfairness of such a system is bound to have [a] chilling effect on a newspaper exercising its right to freedom of expression...and to lead to the danger of self-imposed restraints on publication,” Lord Justice Brooke said in a Court of Appeal libel case last year against the Telegraph Group. Nothing should deter the media from responsible investigative journalism which was of “especial importance in the war against terrorism”, he said.

The “only way to square the circle”, he suggested, would be for the court to make a “cost-capping” order at an early stage of a claim, fixing a maximum amount, including any success fee, that could be recovered by a successful claimant. Following his comments, the Department for Constitutional Affairs issued a consultation paper in June 2004, in which it discussed the flaws in the CFA regime, but failed to propose any solution. Lord Hoffmann has now suggested that new legislation may be needed if the government is to comply with the right to freedom of expression that is enshrined under the European Convention on Human Rights.

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Bagehot

For whom the school bell tolls

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Education reform teaches the Tories how to attack Labour

THE day before the government published its “pivotal” plans to shake up secondary schools, a group of parents was herded into Downing Street to hear the prime minister explain his thinking. What they got was vintage Blair. First Mr Blair constructed a “narrative” to show how what was coming fitted seamlessly with all the wonderful things he had already accomplished. Then he “triangulated”, attacking his critics on both the left and the right by contrasting their ideological blinkers with his own clear-sighted pragmatism. Nice try.

The truth, as Mr Blair knows, is both more complicated and considerably more dangerous. Mr Blair was justified in claiming that some things in Britain's schools have improved—given a near doubling of spending since 1997 it would have been surprising if they hadn't. There are lots of shiny new buildings and lots of well-qualified new teachers. Despite grade inflation, the improvement in GCSE and A-level results is not entirely illusory. But although fewer schools are officially failing than in 1997, far too many are plagued by low aspirations and depressing mediocrity that condemns the mainly poor children who attend them never to escape their backgrounds.

A more honest “narrative” from the prime minister would include a recognition that for several years he had too much faith in his ability to drive up standards from the centre. Even when he did come to realise the importance of creating structures that devolved real powers to parents and encouraged individual schools to compete and diversify, he underestimated the power of footdragging local education authorities (LEAs) to thwart the government's intentions.

Mr Blair's attempt at “triangulation” doesn't quite wash either. It's not just the “left” that is suspicious of the prime minister's determination to open the way to new providers in both health

and education, but ordinary, mainstream Labour MPs, too. Last weekend the deputy prime minister, John Prescott, took the unusual step of telling journalists about his fears that the white paper would lead to “two-tier” provision. Never mind that Britain already has just that thanks to middle-class parents who bid up the price of houses near good state schools or opt to go private when all else fails. Like others on the Labour benches, Mr Prescott resents any challenge to his prejudices.

In a revealing radio interview this week, the last-but-one education secretary, Estelle Morris, expressed her misgivings, while David Cameron, the Conservatives' education spokesman and crown prince, voiced his support for what the prime minister was trying to do. Mr Blair says the “right” attacks him for not going further, especially in its desire to see a return to selection by ability at 11. But what Mr Cameron actually said is that real autonomy for schools should include allowing them a greater say in determining their admissions policy.

If selection were not such a taboo for the Labour Party, the differences between Mr Blair and Mr Cameron would be a good deal slighter than between him and Lady Morris. Mr Cameron claims, entirely plausibly, that the self-governing trust schools that Mr Blair wants to become the norm have a remarkable resemblance to the Tories' own grant-maintained schools, which Labour abolished in a fit of ideological pique. When Ruth Kelly, the rather unimpressive young education secretary, queasily announced the government's plans, the cheers were from gloating Tories rather than her own backbenchers.

This is a tricky situation for Mr Blair, but for the government (which may no longer be quite the same thing), it carries a real threat. The Conservatives have at last realised that the best way to hurt Labour is by trying to prise Mr Blair apart from his party. Their argument, as deployed by Mr Cameron, is that Mr Blair wants to do the right (Tory) thing, but he has left it too late. With his power declining as the unannounced day of his departure draws closer, he is held back by his party and the brooding chancellor next door.

The prime minister's (real) supporters also sense the fragility of his position. The implication of last week's embarrassing deal with the unions over public-sector pensions was that Mr Blair could not fight on that front while trying to reform the nation's schools. And fight he will clearly have to.

In some ways the education white paper is more radical than has been generally realised. Although it pays lip service to a new role of LEAs as commissioners rather than providers of education services, the reality is that they are being stripped of most of their powers. The provisions to accelerate the closure and replacement of failing schools are draconian. A powerful new schools commissioner will work with schools to help turn them into trusts, while the vital capital allocations for extending existing schools or setting up new ones will be at the behest of the recently appointed Richard Bowker, the former chief executive of the Strategic Rail Authority and a diversity enthusiast.

And Gordon says nothing

Some Labour MPs are hostile; many more are uneasy and will become deeply so when they read the fine print of the legislation. The cabinet is becoming fractious and ill-disciplined as was demonstrated by this week's spat over how much further to extend anti-smoking laws. Wanting neither to be labelled anti-reform nor to appear over-supportive of the prime minister, Gordon Brown, as usual, says precisely nothing.

If the prime minister has to choose between diluting the reforms he believes are crucial to his legacy and implementing them with the help of the Tories, he may well think the latter is the lesser evil. Nor will it worry him if he has to stay on for three years to see them through. But it

does not bode well either for the government or for the smooth transition of power the Brownites yearn for.

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Product placement

Lights, camera, brands

Oct 27th 2005
From The Economist print edition

Allstar

Product placement is rapidly blurring the line between content and advertising

NEAR the beginning of “Lost”, an American television drama about a group of plane-crash survivors on a Pacific island, a silver attaché case made by Zero Halliburton takes centre stage. No matter what the characters do to try and force their way into it, only the key to the case finally reveals its contents. This is product placement to die for.

In 2004 the value of product placement in American television grew by 46%, according to PQ Media, an alternative-media research firm. Adding in films, magazines, videogames and music as well as TV, the market was worth $3.5 billion in 2004. Leslie Moonves, chairman of CBS, a broadcast-television network, recently said that three-quarters of all scripted prime-time network programmes will soon contain paid product placement. The growth is occurring because advertisers reckon that it helps to sell their brands, and television firms are desperate for extra money as some of their traditional advertising moves to the internet and elsewhere.

When Channel 4, a British broadcaster, started showing “Lost” in August, it had to decide what to do about the attaché case, because showing products on television for money is mostly illegal in Europe. In the end, it left the incident in, reasoning that British viewers would not recognise the product, or its placement. Such dilemmas are about to disappear. The European Commission will soon alter its laws to allow product placement. It has accepted its television producers' arguments that Europe's ban puts them at a disadvantage to Hollywood, where product placement is an important source of extra funding.

The phenomenon is not new. In the 1930s, Procter & Gamble started broadcasting “soap operas” on the radio featuring its soap powders, and tobacco brands have long used films and TV to lend

glamour to smoking. But advertisers are pushing their way into content far more aggressively than ever before. This is chiefly because they doubt the effectiveness of 30-second spot advertisements. Increasingly, viewers are using personal video recorders to skip them, or are choosing to pay for content without commercials.

Even books now carry product placement, and Broadway musicals too. Newspapers are under pressure to do the same, but are mostly holding out. Last week, the American Society of Magazine Editors decided not to change its rules to allow titles to blur the line between content and ads, as many advertisers had hoped it would.

In the film industry, a lot of product-placement deals are made in return for a brand spending large sums marketing the association with the film, as well as for hard cash. Advertisers are becoming increasingly pushy. Brand owners do not just want their car in the film, complains the head of product placement at a film studio, they also demand tickets to the premiere and for the stars to be photographed in front of their brand boards.

In television, the fastest-growing area of the market for product placement, advertisers and TV firms are trying to work out a more structured and standardised business model. Most placements are currently done on a barter basis. An advertiser will agree to lift its spend on traditional 30-second spots around a show, for instance, in return for product placement inside it.

The tricky part is working out exactly what product placement is worth. At the moment, no-one knows how to price it. So far it seems to have the biggest effect when accompanied by traditional ads. The Coca-Cola Company, for instance, found that audience recall of its ads during “American Idol”, a reality show full of Coke placements, was 49% higher than during other programmes.

Oh for the wings of Dove

One of the key variables, says Alan Gould, co-CEO of IAG Research, an advertising-industry monitor, is how much other product placement there is in the show. In some there is so much “clutter” that the value to any one brand may be limited. Another important factor is whether the central character touches the product: is it thereby a “hero placement”, or further in the background?

Product placement is riskier than conventional advertising. Early this year, Unilever, a consumer-goods firm, integrated its Dove body wash into “The Apprentice”, and candidates competed to design a new ad campaign for the product. Unilever's executives were worried when one of the teams came up with an idea full of sexual innuendo and a gay theme.

Some people think that paid product placement is sinister, and that it should be banned, or at the very least clearly disclosed in credits at the end of a programme. German viewers, for instance, are particularly angry about it because several broadcasters this year have been found to have accepted illegally money for product placement. The European Commission says it will allow product placement in fiction, but not in news or factual material, and will require that broadcasters label it clearly. America's Federal Trade Commission, on the other hand, which regulates advertising, rejected a call from a consumer group called Commercial Alert this year to require disclosure.

Most people do not mind having their content stuffed with products as long as it is skilfully done. There have been shows where it has turned viewers off, such as “The Restaurant”, a reality show on NBC in 2003-04 with lots of clunky placements. Product placement is still a small source of revenue for media companies and they would immediately stop it if they thought it was damaging ratings. But the more skilled advertisers become at it, the less likely that is to occur.

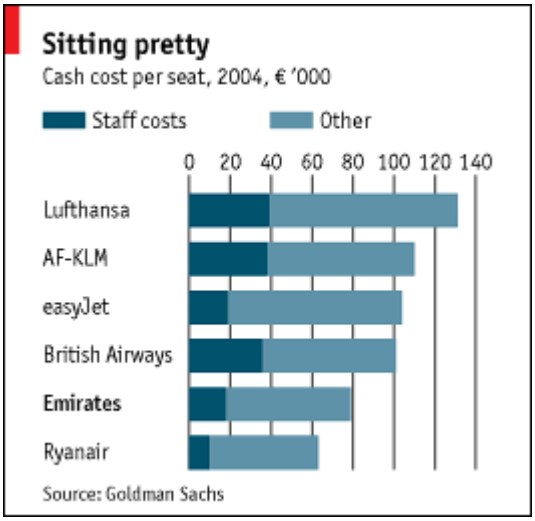
Emirates Airline

EasyOz

Oct 27th 2005
From The Economist print edition

Low cost is coming to long-haul flights. Next could be low fares

Get article background



UNTIL now the received wisdom in aviation was that low-cost, no-frills carriers would be mostly limited to short journeys, with a few exceptions such as JetBlue's flights from New York to the west coast of America. The argument goes that the business model just does not fit longer flights when passengers want frills, such as food and entertainment. On the cost side, long flight times and fuel bills eat away at the savings made by having swift turn-arounds at each end. Several attempts to launch long-haul low-cost airlines have failed to take off.

But low-cost, long-haul flights already exist, on Emirates Airline, a fast-growing carrier based in Dubai. True, Emirates feels more like a classy long-haul carrier, with comfortable cabins and attentive staff, and it has yet to offer rock-bottom fares. But an analysis of its costs (see chart) shows it is closer to Ryanair, Europe's leading no-frills carrier, than to British Airways (BA), Air France-KLM or Lufthansa. Goldman Sachs, an investment bank, also calculates that its profit-per-seat matches that of Ryanair, which is twice the level of Lufthansa and two-fifths more than BA.

No wonder Tim Clark, the president of Emirates, forecast earlier this year that it would be only a matter of time before “the short-haul low-cost model migrated into long haul”. Writing in *Airline Business*, a trade magazine, he envisaged a version of the upcoming Airbus A380 super-jumbo carrying 760 passengers, all in economy class, buying coffee and food at self-service counters and paying for access to in-flight entertainment or even gambling. The 15-20% lower operating costs promised for such huge aircraft (compared with today's Boeing 747s) could mean flights from Britain to Australia for €400 ($480) return. A stretched version of the A380, which the manufacturer is considering, could seat 870 passengers and provide potentially even lower fares. Already Emirates offers, for instance, flights from London, Paris and Frankfurt to Hong Kong, via Dubai, that are up to 30% cheaper than direct flights operated by BA, Air France-KLM and Lufthansa.

European carriers have been watching nervously as Emirates has expanded its passenger numbers by around 15% each year. Its fleet of 80 aircraft is set almost to double by 2012; it has ordered no fewer than 45 (a third of the total orders for the plane) of the A380 that is due to enter service in just over a year's time. Some industry observers wrongly put the success of Emirates down to subsidy from the government of Dubai. It does enjoy a home base where there are no corporate or income taxes and it has the implicit backing of the ruling family (which owns the carrier) when borrowing. But its real savings come from low staff costs (in Dubai there are no unions and plenty

of cheap labour from India and Pakistan), and round-the-clock operations which lead to high aircraft use. Airport fees are also low. The only steep cost the airline faces is in marketing, not surprising for a carrier with a home base of only 1.5m people. This is why it is a big sponsor of cricket and football in Britain, a key source of traffic.

Air France-KLM and Lufthansa have most to fear from the emergence of this new force in long-haul aviation. Dubai is not only a holiday destination in itself, with over 5m visitors a year, but it has profited from its location halfway between Europe and East Asia to build a new kind of global hub, connecting cities in Europe with those in Asia.

The only clouds in Emirates's future could be rival Middle East carriers such as Etihad in Abu Dhabi and Qatar Airways farther up the Gulf. These have spotted the growth of Emirates, and their host countries are happy to pour petrodollars into expanding their operations. The resulting over-capacity could lead to a price war that might sap profits at Emirates. But that would make cheap travel between Europe and Asia even more likely.

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Wal-Mart

Be kind to be cruel

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The twist in a tale of seeming generosity

EVEN before the all-important Christmas shopping season starts, Wal-Mart seems to be sporting a Santa suit. Normally the world's biggest retailer is known for giving its non-unionised employees short shrift on benefits, which helps keep its operating costs low and prices cheap. But this week the company claimed to be mending a few of its ways. It is cutting health-care premiums—to as low as $11 a month for some employees. Greener packaging and the use of renewable energy are also on the way. Oddest of all, Wal-Mart says it will start lobbying for a higher minimum wage.

What has come over the beast from Bentonville? It is still growing like crazy—it plans to open almost 300 new supercentres in its next financial year—but its image is sorely in need of treatment. Better health care, organic products on the shelves, and waterless urinals (at the experimental stage now) are clearly part of a bid to woo back middle-class customers. Many of these righteously boycott Wal-Mart because of its perceived ill-treatment of its workers. Less than half of its “associates” have health insurance; 5% have to resort to Medicaid, the increasingly cash-strapped government programme for the poor. All this was briefly forgotten last month when Wal-Mart made an extra effort (and gained good publicity) by helping victims of the hurricanes in the southern states of America.

But wait. Lest anyone think the beast has changed entirely, the *New York Times* this week unearthed an extraordinary internal memo from Wal-Mart's executive vice-president of benefits to the board of directors advocating ways to slash benefit costs, which had been growing at the “unacceptable” rate of 15% a year. Among them: “Design all jobs to include some physical activity (eg, all cashiers do some cart gathering)”. This is seen by the unions as a ruse to avoid employing the infirm. Other recommendations included making employees pay more for their spouse's health care, and cutting “investment” in profit-sharing and 401(k) retirement programmes from 4% to 3%. The rationale for the latter is that “retirement is a low-importance benefit for associates”.

Unions are outraged. Chris Kofinis of WakeUpWalMart.com, a project of the United Food and Commercial Workers, calls the memo “one of the most disturbing documents I have ever read”. It exposes the firm's other announcements, he says, as “cynical publicity stunts”. Critics will soon have more to feast on when a stark documentary called “Wal-Mart: The High Cost of Low Price” is released on November 4th. It is unlikely to show the company in a Santa suit.

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Economist.com BUSINESS

Business continuity planning

When lightning strikes

Oct 27th 2005
From The Economist print edition

How to maintain business as usual in unusual times

AP

Just a temporary upheaval

COMPANIES' contingency planning used to consist of little more than duplicating IT facilities in case their systems went down or the hardware in their basement was flooded. Today, however, firms are aware that they need to think about many more potential disruptions. Hardly a week goes by without a new threat. Last week, the government of New Zealand issued a pandemic planning guide for businesses, suggesting how firms should prepare for an outbreak of avian flu. Gartner, a large IT research firm, has advised companies to consider whether their systems could continue if up to 30% of their staff were to be absent from the workplace.

This week yet another hurricane swept across the southern states of America. Every time a Katrina, Rita or Wilma wreaks her havoc, firms around the world worry that a vital supplier may have been knocked out of their increasingly global supply chains. In a recent survey by Harris Interactive, a polling firm, and FM Global, an American property insurer, financial executives in Britain and North America said that the top threat to their revenues came not from terrorism or natural disasters directly, but from a breakdown in their supply chain.

The effect on Ericsson, a Swedish mobile-phone company, of a fire in a New Mexico chipmaking plant belonging to the Dutch firm Philips, has become a legend. The fire, in March 2000, started by a bolt of lightning, lasted less than 10 minutes, but it caused havoc to the super-clean environment that chipmaking requires. Ericsson, unable to find an alternative source of supply, went on to report a loss of over $2 billion in its mobile-phone division that year, a loss that left it as an also-ran in an industry where it had once been a leader. The lesson was not lost on other firms with far-flung global supply chains. General Motors, for example, now systematically tracks the geographic origin of all the bits that go into making its cars.

The growth of outsourcing has added to the complexity of the issue. Removing back-office business services to low-cost (and frequently more hazardous) locations leaves firms vulnerable to hard-to-monitor disruptions in those faraway places. Susir Kumar, chief executive of Intelenet, an Indian outsourcing firm that is 50% owned by Britain's Barclays Bank, says that Indian firms are in fact more diligent about continuity planning than firms in the West—partly because disruptions there are more frequent (so they get more practice), and partly because costs are so much lower they can afford to duplicate more facilities. Indian outsourcers say there was little consequence for their clients from the flooding in Mumbai in July.

Firms around the Gulf of Mexico also get plenty of practice at business continuity plans that kick in when the storms blow in. Companies such as Boeing, UPS and Wal-Mart, which have thousands of employees in and around Houston, for instance, were up and running again a couple of days after Hurricane Rita hit the city in September. NASA's flight controllers were away from their desks for six days, during which time control of the international space station passed seamlessly to colleagues in Moscow. Good planning can save both money and lives.

For businesses around the Gulf, property damage is the least of their worries. Relatively cheap techniques now minimise the damage: using top-quality roof fastenings, for example. The biggest challenge during this year's spate of hurricanes has been keeping in touch with employees forced to flee to new locations. Mobile phones proved unreliable as masts were blown down, and Boeing, Southwest Airlines and UPS are among those companies that have modified their procedures as a result, relying more on e-mails, hot lines and their own websites to keep in touch with distant employees.

While most big companies are continually refining their business continuity plans, many smaller firms are not. Recent research by AXA, a European insurer, found that 46% of small and medium-sized businesses in Britain do not have a business continuity plan of any sort, despite being alerted again to the risks of disruption by this summer's terrorist bombings in London. For some, the task is too daunting; the risks too universal. They prefer, says AXA's Douglas Barnett, to assume “they can deal with disruptions as and when they happen.”

In a book published this month (“The Resilient Enterprise” by Yossi Sheffi; MIT Press), the author, a professor of engineering systems at MIT, gives some guidance to firms that are shy of examining these risks. “Large-scale disruptions”, he says, “rarely take place without any warning ”. By carefully monitoring and analysing near-misses, the airline industry has avoided many a crash. Likewise, says Mr Sheffi, “learning from small incidents can help organisations correct the conditions that lead to accidents.” Lightning can strike twice in New Mexico.

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InBev

Head to head

Oct 27th 2005 | LEUVEN, BELGIUM
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The perfect pint, served at home

AFTER a hard day at the office, John Brock can return home and pour himself a beer. Unlike most people, though, he can serve himself a draft Stella Artois exactly as Belgian bartenders do: cooled to the perfect 3°C and with a frothy head skimmed to the brim of a chalice-shaped glass. Such a privilege might be expected when you are the boss of InBev, the world's biggest brewer. But it is a privilege that Mr Brock hopes many more beer drinkers will soon enjoy.

So does his Dutch rival Heineken, which has begun legal proceedings against InBev and its partner Philips, a Dutch consumer-electronics firm, which jointly developed the PerfectDraft machine that Mr Brock has in his home. Launched last year in Belgium, it is now being introduced across Europe. But Heineken claims it breaches patents that it holds on BeerTender, a similar machine that it developed with Krups. InBev and Philips have denied the claim.

Whatever the outcome of this legal spat, it shows how seriously brewers are trying to increase sales and move beer upmarket. In most mature economies, beer sales are flat or declining as people drink more wine and spirits. The high-growth markets are now in Latin America and in China, which has become the world's biggest beer consumer, ahead of the United States, Germany and Brazil. However, annual per-person consumption in China is only 27 litres, and in Brazil 49 litres, whereas in the United States it is 83 litres. So the big brewers see plenty of further growth in these developing markets, although profit margins may be slim because competition there is fierce.

Mergers have been designed to help firms tackle these markets. InBev was formed in August 2004 by the $11 billion merger of Belgium's Interbrew and AmBev, Brazil's biggest brewer. The combined group had sales of 166m hectolitres last year, according to Canadean, a research company, putting it ahead (by volume) of SABMiller—which in July paid $7.8 billion for Grupo Empresarial Bavaria, the leading brewer in Colombia, Ecuador and Peru. America's Anheuser-Busch is third and Heineken fourth.

In terms of the value of sales, however, InBev falls to third place. This is why its strategy now is to go from “biggest to best” and achieve the highest profit margins in the business. The old Interbrew was, admits Mr Brock, an “acquisitions machine” (in 1990 it was only the world's 17th largest brewer). To drive profits, the company will rely more extensively on its portfolio of well-known brands, which Mr Brock aims to use to “make beer more relevant, more exciting.” This means persuading drinkers, especially young adults, to buy more premium and imported beers, which carry higher margins.

This is a marketing job, and one for which Mr Brock, an American citizen, is well prepared. He started his career at Procter & Gamble before joining Cadbury Schweppes, two marketing giants. (He joined Interbrew as chief executive in February 2003.) These days the big brewers are using marketing tricks learnt from the consumer-goods industry: for example, they are launching local brands into new markets where they can be seen as premium products; they are producing so-

called line extensions—versions of existing brands, such as low-calorie beers; and they are coming up with more innovative packaging, such as the controversial draft-beer dispensers for the home. The InBev machine uses mini kegs containing six litres (10.6 pints) of InBev's Jupiler or Stella Artois beers.

InBev is now pushing Stella Artois and its premium German beer, Beck's, as global brands: Stella Artois was launched in Brazil in June. The company has also put Brahma, one of AmBev's main beers, in a smarter bottle, and it is beginning to roll it out as a premium global brand. Speciality beers are part of the formula too, such as Hoegaarden, a Belgian “white” beer. Meanwhile in Brazil, Bohemia, another AmBev brew, is being marketed as an “abbey” beer. Like InBev's successful Leffe, Bohemia is made under licence from abbeys. Monks, it seems, have good bees, brands and beer.

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Economist.com BUSINESS

South African diamonds

Rough and tumble

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A controversial bill to keep more rocks at home

CAN South Africa put more shine on the diamonds that it mines? It is the world's fourth-largest producer by value, with 12% of global output. Yet its cutting and polishing sector is small, employing about 2,000 people. Most of its stones get exported in rough form, to be cut in Belgium, China, India or Israel.

Now the government is keen to create jobs and add value to the country's diamond exports by boosting the local cutting and polishing industry, and by having more jewellery-makers at home. This seems like a good idea. But the way it is planning to go about it is raising eyebrows in the industry. A bill now before parliament includes provisions to set up a state diamond trader and exchange, which would manage imports and exports, buying a share of local production for the local cutting market. An export levy on rough diamonds is also being planned.

The mining industry argues that this is likely to hurt extraction and do little to develop the downstream diamond industry, which needs incentives such as tax breaks, rather than regulation, to flourish. Meanwhile, the export levy would hit diamond mining. The Chamber of Mines of South Africa reckons that the proposed law could create up to 1,000 jobs in cutting and polishing diamonds, but destroy 12,000 in mining them. Small diamond producers are likely to suffer most.

Critics also say that the private sector is doing a good job of buying and selling diamonds, and that the government should not meddle. De Beers, which extracts about 90% of South Africa's diamonds, says that more than nine out of ten carats produced locally are of relatively low value, in which South African buyers are not showing great interest. The mining giant points out that the mix of rough diamonds that get sold back in South Africa—after having been sorted and pooled in London by its Diamond Trading Company—are on average better and more expensive than those produced at home.

Small producers sell their production on local diamond exchanges, but most of it still does not get cut and polished in South Africa. The Chamber of Mines points out that labour costs are much lower in India or China. It estimates that, with a 15% export levy, less than 5% of the local production could be cut profitably at home.

The government is not convinced that this is indeed the case. It wants to make more diamonds available and monitor the local appetite for them. At this stage, the level of the export levy, and how much the state trader will actually buy, are still to be decided. The government is keen to have the bill passed by early November. If it meets that deadline, it will be a rough and unpolished piece of legislation.

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Economist.com BUSINESS

Employee share options

No compensation without cost

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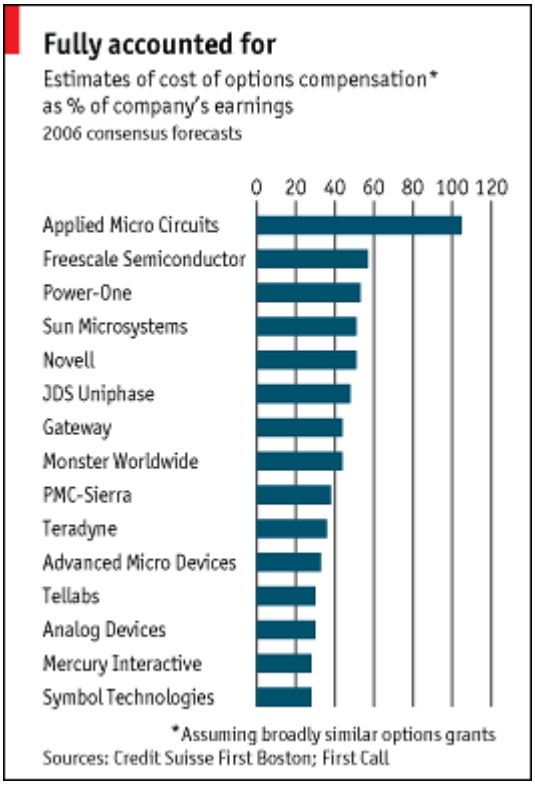
As corporate America prepares to account for employee share options, they are losing their appeal

MANY of America's top executives have long claimed that the expensing of employee share options would rob American capitalism of its magic. Now their claim is about to be tested. Firms must expense options from the first financial year beginning after June 15th 2005. For many American companies, the cost of their options will have to be reflected in the profits that they report for the first quarter of 2006.



For years the clout of the business lobby in Washington has prevented this happening. In 1994, the Financial Accounting Standards Board (FASB) dropped a proposed option-expense rule after Congress voted against it. But the FASB revived the rule in 2004, and this time the business lobby lost. Share options no longer seemed unambiguously attractive, not least because of their part in stimulating America's turn-of-the-century corporate excess. Several leading businessmen publicly supported expensing them—not least, America's favourite boss, Warren Buffett.

A few enlightened firms already do it voluntarily, including roughly one-quarter of those in the S&P 500 index. But others are choosing to remain in denial right to the end. Firms are currently giving guidance to Wall Street analysts about the profits they expect in the first quarter of 2006. But, according to David Zion and Bill Carcache of Credit Suisse First Boston, there are only 96 firms out of the S&P 500 for whom Wall Street's consensus estimate reflects the cost of options.

What would happen to the consensus estimate if the cost of options were included? According to calculations by Messrs Zion and Carcache, who assume options grants similar to this year's, the S&P 500 firms will report total options expenses of $33 billion in 2006. Although a lot of money, this would reduce the current consensus estimate for total S&P 500 profits by only 3%. However, the use of options varies enormously. In some industries, profits will be hit particularly hard. Including the cost of options would lower the consensus 2006 profit estimate for the semiconductors and semiconductor-equipment sector by 23%, calculate Messrs Zion and Carcache. And, according to their rough estimates, a handful of companies would see their profits fall by over 50%, including Sun Microsystems and Novell, while one firm, Applied Micro Circuits, would swing from profit to loss (see chart).

Fears are now growing that firms with larger options costs will try to disguise their impact by reporting a “pro-forma” profit number that excludes the cost of options, alongside the options-expensed profit figures that they have to calculate under Generally Accepted Accounting Principles (GAAP). Pro-forma profits are, supposedly, a firm's measure of its core continuing profitability, excluding the impact of exceptional one-off gains and losses. During the stockmarket bubble that burst in 2000-01, firms extensively abused pro-forma numbers. After the bubble, pressure for better accounting led to an encouraging reduction in the difference between GAAP and pro-forma numbers. But the difference between them has been growing again.

Although there is no single correct way to calculate the accounting cost of an employee share option, and the FASB's method is a compromise, options are clearly not an exceptional item. So they should not be ignored for the purposes of pro-forma profits. Yet firms might get away with doing so, reckons Bruce Brumberg, editor of a website, myStockOptions.com. There is currently much confusion about how to use data on the cost of options, he says, particularly when making comparisons with past years. In these muddled circumstances, pro-forma guidance from firms that excludes options costs may be accepted uncritically. Ominously, earlier this month Google, which not so long ago boasted that it expensed its options, said that it will now report pro-forma profits that exclude options costs.

Even if options costs are fully reported, their impact will certainly be much less dramatic than seemed likely a few years ago. (According to Goldman Sachs, expensing options in 2001 would have reduced S&P 500 profits by almost 15%.) Two key things have happened since then. First, profits have grown far more than anyone expected, thereby reducing the relative importance of options costs. Secondly, the value of options granted has fallen sharply. Part of the decline has been due to the demise of flakier companies that appeared during the bubble, which tended to be big users of options. Another factor has been the decision of former big users (such as Microsoft) to seek different methods of employee compensation. According to a recent report by Deloitte, a firm of accountants and consultants, the decline in the use of options is much larger in public companies than in smaller private firms. Start-ups, it seems, are continuing to pay their employees in this way.

Is the decline in the use of options to any extent a reflection of the fact that expensing them is imminent? So far, there is no evidence that the prospect of expensing has caused firms to which options are suited to abandon them. Perhaps when expensing begins, they will scrap their options. But just as likely, they will weigh up more accurately whether granting options is a good use of resources. As Mr Buffett wrote in his latest letter to his firm's shareholders, “we cheer arrangements that motivate managers, whether these be cash bonuses or options. And if a company is truly receiving value for the options it issues, we see no reason why recording their cost should cut down on their use”.

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Economist.com BUSINESS

Face value

Fighting to the top

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Thomas Fischer, Germany's most colourful banker, may become its most influential

Landov

“GERMANY'S most colourful banker”, may not be the world's most sought-after accolade, but it is one that is often given to Thomas Fischer, a man who rarely stays in one job for long. He has had two incarnations at Deutsche Bank, Germany's biggest, and one at a public-sector bank in Stuttgart: each time bowing out when his advancement was frustrated. That did not deter politicians in North-Rhine Westphalia from courting and hiring him in 2003 as the potential saviour of WestLB, a troubled Landesbank. (Landesbanks act as wholesale banks for the publicly owned savings banks in their region.)

Mr Fischer's style is not to everyone's taste. He vaunts his prowess as a pugilist, favours suits with improbably wide pinstripes, and puffs large cigars. Many bankers privately think him a clown, but he has boxed his way right to the centre of the upheaval in Germany's public banking sector, which accounts for nearly 50% of the nation's banking assets, both as chief executive of WestLB, once Germany's third-biggest bank, and as chairman of the Association of German Public Banks. The question now is, will he make a difference before he bows out in search of another challenge? He has said himself that if WestLB fails to reach its targets by 2007, it will be time for it to find another boss.

When he arrived, the bank was reeling from a private-equity scandal in which shoddy supervision had led to loony investments in British cinemas, a TV rental firm called Box Clever, and a new Wembley sports stadium. Top bank executives had their brains apparently anaesthetised by the charms of Robin Saunders, a blonde American who led the private-equity business. Mr Fischer dragged WestLB away from fantasy and back to its core role, serving the North-Rhine Westphalian savings banks with wholesale products (such as currency and interest-rate protection). He has also sold the bank's equity stakes in Boullioun Aviation, Mid Kent Water, whisky-maker Whyte and Mackay, and TUI, a troubled tourism business.

But the biggest challenge hitting Germany's public banks this summer was the abolition of the state guarantees which had given them an automatic triple-A or double-A credit-rating. From July 19th the banks have been rated according to their own strength, backed by only the possibility—no longer the certainty—of support from their public owners. Mr Fischer, by cajoling his local savings banks, which own 60% of WestLB, managed to gain a rating of A-. That is despite a running dispute with Brussels over €1.4 billion ($1.7 billion) of its capital judged to have been an unfair subsidy from the German state.

Technology has begun to make a nonsense of the regional principle which has traditionally forbidden public banks from encroaching on each other's turf. Dietrich Hoppenstedt, head of the German Savings Bank Association, is fighting a rearguard action against internet “direct” banks and other nationwide sales efforts that are resulting in public banks from one region poaching business from public banks in another. Bayerische Landesbank in Bavaria, for example, has an online bank with branches in some eastern German states; Landesbank Hessen-Thüringen has an internet bank which is building a nationwide base of retail clients. Mr Fischer suggested that WestLB should start a direct bank in competition, but his savings banks slapped him down.

Common sense says that the regional principle will not survive. Economies of scale increasingly demand the use of common platforms and marketing efforts. But Mr Hoppenstedt, due to retire next year, is determined that the savings banks and the Landesbanks should co-operate and not compete head-on. He has called for a tribal gathering in Berlin on November 7th, at which a survival strategy will be mapped out. His plans involve nationwide joint marketing of some savings-bank products and perhaps the merger of some Landesbanks. The Landesbanks are already forming clusters, via cross-shareholdings, but there is a reluctance by regional politicians to see their Landesbank, however small and uneconomic, disappear into the maw of another.

Risk controller

Mr Fischer joined Deutsche Bank in 1985 from the battery-maker Varta after completing part of his education in Canada, where he mastered Irish-American banter. Risk control is his thing: his last job at Deutsche Bank was as board member in charge of risk. In 2002 he failed to prevent Josef Ackermann, now its chief executive, from imposing an Anglo-Saxon management structure on the bank, and he quit the institution for the second time. For a while he advised Bayerische Landesbank on its loan exposure to Formula One, and the private-equity firm Cerberus on investments in Germany.

Mr Fischer rarely throws the first punch in any scrap, but he is quick to respond if someone else does. On reports in September that Landesbank Baden-Württemberg wanted to increase its 20% stake in Trinkaus & Burkhardt, a private bank based on WestLB's home turf of Düsseldorf, Mr Fischer did not hesitate. “If a certain member of our organisation from another region gets hold of Trinkaus & Burkhardt then that is the end of peace among the public banks,” he declared. Since then there has not been a peep out of Siegfried Jaschinski, the head of Landesbank Baden-Württemberg and a former Deutsche Bank colleague. HSBC, which owns 73% of Trinkaus, is in any case not selling.

Mr Fischer is not as belligerent as he sometimes sounds. But perhaps even at his most tactful he will not be able to transform WestLB. He may not have time: there is speculation that he could be called to another fight. Mr Ackermann was put on trial last year, along with five others, for approving extraordinary bonuses after Mannesmann's takeover by Vodafone in 2000. They were acquitted, but an appeal hearing last week may lead to a retrial too embarrassing for Mr Ackermann and his bank. Mr Fischer has been touted as a possible successor.

Economist.com FINANCE & ECONOMICS

China's banking industry

A great big banking gamble

Oct 27th 2005 | BEIJING, HONG KONG AND SHANGHAI
From The Economist print edition

Reuters

Reforms of China's banking system have not gone nearly far enough

Get article background

IT IS a staggering thought: communist China now has a bank more valuable than Barclays, American Express or Deutsche Bank, financial institutions at the heart of Western capitalism. At more than $66 billion following its initial public offering in Hong Kong on October 27th, China Construction Bank (CCB) boasts a larger market capitalisation than any of these three. CCB's listing, which raised $8 billion from foreign investors for 12% of its shares, is the largest global flotation for four years, China's biggest and the biggest ever for a bank. CCB garnered another $4 billion ahead of its float by selling stakes of 9% to Bank of America and 5.1% to Temasek, Singapore's investment agency.

This is quite a transformation for a bank that was technically insolvent less than two years ago and which, despite a hastily applied commercial gloss, is still a government agency, plagued by bad debts and corruption so pervasive that just five months ago its then chairman was arrested for bribery. In private, China's leaders must be marvelling that they have pulled off this sale. Yet their ambitions are far greater. Bank of China (BOC), the second of the “Big Four” state banks, with foreign investors already aboard, is planning a $5 billion foreign listing in early 2006. Industrial and Commercial Bank of China (ICBC), the biggest, is appointing advisers for a $10 billion flotation late next year or in 2007. Many of the smaller joint-stock and city banks now too have foreign investors and are eyeing overseas listings.

Beijing is encouraging this rush to market as the most fundamental step in reforming the economy since Deng Xiaoping opened China to the world in the late 1970s. Since then, the country's banks

have been almost wholly responsible for channelling the population's sky-high savings into industry and investment. Given China's failure to develop healthy stock and bond markets, bank assets have ballooned to almost 30 trillion yuan ($3.7 trillion) in 2004, or 210% of gross domestic product (GDP). That is the highest of any big economy, says Nicholas Lardy at the Institute for International Economics in Washington, DC: India is at 170%, Brazil 160% and Mexico 100%.

Sadly the banks have been disastrous middlemen, lending on government instruction without a view to their profits. They have poured money into wasteful infrastructure projects and kept broken state-owned enterprises (SOEs) afloat. Not only has this created huge non-performing loans for the banks themselves, but also because China's investment is so unproductive, it has to shovel ever more money into its economy to maintain its current growth. Already, China needs almost $5 of fresh capital to generate $1 of incremental output, a far worse ratio than Western countries and even India. In the first quarter of 2005, fixed-asset investment reached an incredible 54% of GDP, 10 percentage points above the household savings rate. No country can sustainably invest more than it saves and China must raise the productivity of its economy.

That is why overhauling its banks is so critical to securing the country's future growth. China's political leaders have an iron commitment to bank reform—a commitment backed with cash. Since 1998, Beijing has injected more than $260 billion into its banks via straight handouts and by allowing the Big Four to shift dud loans into separate state-backed companies. This is about twice what South Korea spent to restructure its banks after the 1997-98 Asian crisis and about what America needed to bail out its savings & loans industry. Mindful of the long paralysis of Japan's indebted financial system, China is pumping in funds before a financial meltdown. Weijian Shan, a director at Newbridge Capital, a private-equity firm which owns a controlling 18% stake in Shenzhen Development Bank (SDB), is impressed: “the government is taking the pain before it is too late, showing it understands that China's economic development depends on a healthy banking system.”

Beijing realises too that money alone will not do the trick. Since 1998 it has raised accounting, prudential and regulatory standards. Before then, the banks could book interest income for up to three years even if it was not being paid; now they can do so for only 90 days—the international norm. In 2002, the old lenient system whereby banks provisioned just 1% of their loans regardless of risk, was replaced by a five-tier classification tying the size of the provision to loan quality. Meanwhile, the central bank's decision last October effectively to lift the ceiling on commercial loan rates should, in theory, allow banks to charge more to riskier borrowers.

The biggest change, though, has been the creation of a central regulator, the China Banking Regulatory Commission (CBRC), carved out of the central bank in 2003. Headed by Liu Mingkang, a respected former president of BOC, the regulator is trying to shift the banks' focus from mindless loan and deposit growth to preserving adequate capital and generating decent returns on it. Lenders that do not meet a capital ratio of 8% of risk-weighted assets (as decreed by Basel I, a global standard) by 2007 face sanctions—including the removal of senior management. The regulator's 20,000 staff are trying hard to ensure compliance. “At every board meeting, the CBRC guy is right there taking notes and pounding the table,” says Stephen Harner, a former diplomat who now sits as an independent director at Hangzhou City Commercial Bank.

The rush for reform

All this has given an urgency to reform efforts. Almost all China's 128 commercial banks have introduced better governance, shareholding and incentive structures, and have added independent directors to their boards. Senior managers are investing in new risk systems and trying to change bad old habits such as having the same person make and approve a loan, a practice that encourages corruption.

The restructuring has been helped by a benign environment. China's economic boom fuelled annual loan growth of almost 16% over the past four years and deposit growth of 18% a year. Lending to consumers, which started only in 1997, has exploded, increasing 123 times to more than 2 trillion yuan ($250 billion) in seven years, says Merrill Lynch, an investment bank. Corporate loans still dominate, but mortgages, car and education loans now make up 11% of the total and 26% of new lending, says Mr Lardy (see chart 1).

Strong revenue growth and offloading bad debts on to the government has inflated bank profitability. Last year, China's 13 biggest banks made net profits of 90 billion yuan ($11 billion) and a decent-looking return on equity (ROE) of almost 11%, says Fitch, a credit-ratings agency. Over half came from CCB, the sector's poster child, which expects net profits of 42 billion yuan ($5.2 billion) for 2005. Though it is only the third-largest lender, aggressive management, leadership in mortgages and the number two position in debit and credit cards have helped it achieve an industry-leading ROE of over 25%.

Meanwhile, the headline non-performing-loan ratio reported by the CBRC fell to 8.8% of total loans by this June, down by half since the end of 2003. CCB looks much cleaner, with a ratio of 3.91%. It has stronger reserves, with loan-loss provisions of 64% of its bad loans compared with 15% average for its peers. Its listing prospectus says that loans to “new” customers (acquired since 2000) are one-third as likely to go sour as those to older clients, suggesting regulations are working. On this basis, CCB looks only a bit worse than developed-world banks.

Well, it would, if that were indeed the true picture. Independent estimates put bad debts at 20-25%, far exceeding official figures. The CBRC itself paints an alarming picture. In an internal report leaked to Shenzhen's *Securities Times*, the CBRC found system-wide bad loans actually rose this year, if a disposal from ICBC was excluded. It expects 30 billion yuan in new bad loans in 2005. And on October 14th having inspected 11 banks, the CBRC concluded that it is “common practice” for banks to ignore regulations and fail to monitor loans, and that bad-loan levels are “not accurately revealed”. Poor accounting means that the banks themselves are unsure of their bad loans. Others do not tell. Lai Xiaomin, head of the CBRC's Beijing office, admits that “when our banks disclose information, they don't always do so in a totally honest manner.”

That bad loans are rising, not falling—Fitch estimates by 8% in the first half of 2005 once government-funded write-offs are excluded—is not surprising. China's banks went on a lending binge between 2003 and 2004, partly to “grow out of” their bad loan problem. Many loans will go sour, as Beijing has moved to curb overheated sectors such as steel, cars and property. If economic growth slows, a new wave of bad loans will hit. In addition, banks carry alarmingly high levels of “special mention” loans, ranked as performing but where a borrower's circumstances have worsened. Even at CCB, these are 14% of the total.

Look at the books

A new surge in bad debts would be bad enough if Chinese banks had the earnings power to absorb them, but they do not. Behind the headline numbers, their basic profitability is very poor. An average net interest margin of 2.36% looks decent compared with the 1.5-2.5% in developed markets. But David Marshall, head of Asian financial institutions at Fitch, argues that Chinese banks need far wider margins to cover the risks typical of an emerging economy. Indonesian banks, for example, boast a 5% net interest margin and Indian banks 3.45%. Meanwhile, Chinese banks are too dependent on loan income. More stable income from commissions and credit-card fees is only 13% of total revenues, half the level at Indian banks and just one-third of Thailand's. And while costs at Chinese banks are low, at 45% of revenues, this reflects poor investment in training and IT, not better efficiency.

Put all of these factors together and the return on assets (ROA) generated by China's banks, at less than 0.5% last year, is the worst in Asia (see chart 2). Granted, they look better measured by ROE, but this too is deceptive. The excellent 25% CCB highlights in its prospectus is really 17% after adjusting for a tax break. More crucially, the sector's 11% reflects inadequate levels of equity (in other words, capital) rather than high returns. The industry has a capital-adequacy ratio of barely 8%. Mr Marshall argues that China's banks should be carrying capital of at least 15-20%, as banks in Indonesia do, to guard against unforeseen risk. If they did, their ROEs would drop to 5% or less—a much truer reflection of their innate level of profitability.

Two sobering conclusions follow. The first is that even a tiny deterioration in business conditions that either reduces margins or increases bad loans would wipe out earnings at China's banks. The second is that even if the economy remains good, the banks cannot generate enough internal capital to support their current levels of loan growth. Ryan Tsang at Standard & Poor's, a credit-ratings agency, estimates that to avoid more capital injections the banks have to generate an average ROA of 2.1%, almost five times current levels.

Clueless lenders

To close that gap will take a fundamental transformation of how Chinese banks operate. The banks simply do not understand how to price risk or spot a dodgy borrower. Neither flexible interest rates nor loan classifications can help if credit officers cannot tell good loans from bad. The current boom has led loan officers to believe the value of collateral always goes up.

The real battle for bank reform will be won or lost in the branches. While reforms have changed much at head offices, they are hard to enforce elsewhere. Guo Shuqing, CCB's new chairman, admitted shortly after he got the job, that “more than 90% of the bank's risk managers are unqualified”—a bold statement from a man wanting to list his company.

Reuters

These are massive organisations to turn around, after all. CCB alone has 14,250 branches and 304,000 employees. Their historic decentralisation makes them especially hard to control. In a book to be published in November, Wu Jinglian, China's most respected economist, notes that until a decade ago provincial branches of commercial banks borrowed funds directly from provincial offices of the central bank and lent them to local customers. They enjoyed “legal person status” and did not require authorisation from head office. Even today, big branches of ICBC have their own English-language websites—emphasising their independence. “Branch managers are kings in China,” concurs Frank Newman, an American who took over as chairman of SDB on behalf of Newbridge earlier this year.

At all banks there is a struggle between head office, which wants to centralise processes, and local staff who are in thrall to

the demands of local officials and industrialists and who disobey their branch managers on whom they depend for their promotions at their peril. Unhelpfully, the branches are being monitored by a regulator that faces the same problems as its charges—too many unqualified staff spread too thinly. Han Mingzhi, head of the CBRC's international department freely admits, “we lack people who understand commercial banking and microeconomics. It is a headache for the CBRC.” The result is that it will take China's banks years to establish proper corporate governance, a genuinely commercial culture and hence decent profitability.

A pyramid of cards

Meanwhile, strategic foreign investors are supposed to bridge the gap—with money, but especially with skills in risk management and advanced financial products. The lure of China's high growth and huge population has triggered an astonishing stampede, attracting some $18 billion in foreign direct investment in China's banks in one year. The first big deal was the $1.7 billion HSBC paid for a 19.9% stake in Bank of Communications (BoCom), the fifth-largest lender. Then came CCB. Since then, a consortium led by the Royal Bank of Scotland has put $3.1 billion into BOC, Temasek another $3.1 billion and Switzerland's UBS $500m, while Goldman Sachs and Germany's Allianz are investing in ICBC. Only Agricultural Bank, the Big Four bank with the deepest problems, has failed to attract a Western investor.

In return, the international banks get a cut-price entry ticket: Bank of America paid 1.15 times book value for its stake in CCB, which has now floated at almost twice book. They also gain access to a branch network and client list they could never afford to replicate, even after World Trade Organisation rules force China to open its domestic banking market fully from end-2006. Every deal is thus accompanied by a joint-venture in savings and insurance products and, of course, credit cards—the Chinese financial market that has every foreign investor salivating.

Only 12m of the 880m bank cards in China are genuine credit cards. So McKinsey, a management consultancy, predicts exponential growth from this segment, and profits of $1.6 billion by 2013. Yet McKinsey also notes that half of existing accounts are unprofitable. Chinese pay their bills in full each month, show little loyalty to brands and are unimpressed by foreign-backed offers. Ron Logan, head of HSBC's credit-card venture with BoCom, says acquisition costs are soaring as competition heats up, with everything from DVD players and holidays used to entice customers, further eroding profits. Jean-Jacques Santini of BNP Paribas, which just bought one-fifth of Nanjing City Bank, warns investors: “expect to lose money on credit cards for the first three or four years.” The only way for investors to make decent returns in the short term is by betting on a big rise in post-IPO share prices. Everything else they take on trust.

A very Chinese welcome

Meanwhile, given limited ownership rules, foreign banks can have only a modest influence on strategy or operations at their Chinese partners. Newbridge is an exception since it has won genuine management control of SDB, which is small and has a widely dispersed ownership. HSBC's vastly greater size compared with BoCom, means it might, in time, have a significant say. The rest are restricted to one or two board members each, while the appointment of senior management remains with the Communist Party. “Can China's banks be fully reformed while staying under government control? I doubt it,” says Mr Marshall.

To reform its banks properly, China must allow foreign takeovers. And its banks must be allowed to merge and fail. Yet even if Beijing raises cumulative foreign-ownership limits above the current 25% next year, as the CBRC expects, it is unlikely to relinquish control of a major bank. Worryingly, the CBRC seems ambivalent about foreign participation. Mr Han says he doubts the wisdom of raising the ceiling on foreign investment “if we don't get something in return”. Yet as banks in Poland and the Czech Republic discovered, preventing foreign takeovers simply delays bank reform and means more costly bail-outs. A stockmarket listing cannot really help while the state remains in charge: minority investors can do little to change poor corporate governance or influence strategy.

Instead, China is gambling on going it alone. By rushing poorly reformed banks to market and sucking in a bit of money and know-how (not to mention greater scrutiny) from foreign investors, it hopes to improve them sufficiently and sufficiently rapidly before the economy runs into a headwind. The size of that gamble should not be underestimated.

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Economist.com FINANCE & ECONOMICS

Federal Reserve

Betting on Ben

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From The Economist print edition

The likely new chairman of America's Federal Reserve Board is a first-rate academic. Will he be a similarly good central banker?

FOUR years ago, Ben Bernanke was a professor of economics at Princeton whose policymaking experience consisted of a stint on the local school board. On February 1st, barring any unforeseen hiccups in his Senate confirmation, he will become the most powerful central banker in the world, replacing Alan Greenspan as chairman of the Federal Reserve Board.

Nominating Mr Bernanke on October 24th, George Bush said he was the “right man” to replace a “legend”. Wall Street seems to agree. Financial pundits have heaped praise on Mr Bush's choice. Stock prices rose on the news, the dollar held steady and although bond prices fell—yields on ten-year Treasuries hit a six-month high of 4.5% on October 25th and rose thereafter—they had seen worse. When Mr Greenspan was named as Paul Volcker's successor in 1987, stocks fell and bonds had their worst day in five years.

What explains the Bernanke bullishness? Relief, for one thing. Many on Wall Street fretted that Mr Bush might opt for a financial version of Harriet Miers, his recent Supreme Court nomination, to succeed Mr Greenspan, favouring ideological fealty more than independence and ability. Instead, he chose a man with dazzling academic credentials, a short but successful stint as a Washington policymaker and little partisan baggage.

Mr Bernanke is one of America's foremost monetary economists. He was a Fed governor between 2002 and 2005, moving from that job to become chairman of Mr Bush's Council of Economic Advisers. Whereas Mr Greenspan was regarded as a partisan figure before he became chairman of

the Fed, few of Mr Bernanke's academic peers even knew he was a Republican until he moved to the White House.

More important, financial markets are calmer than when Mr Greenspan took over. Wall Street thinks the central bank's commitment to fighting inflation is so entrenched that only a wacky outsider could shake it. Mr Bernanke is no such wing nut. “My first priority will be to maintain continuity with the policies and policy strategies established during the Greenspan years,” he said on October 24th.

In many ways that will be easy. For all the superficial differences, the bearded academic has much in common with the owlish Washington insider he will probably succeed. Both believe in an activist Fed; both focus on the link between the pace of aggregate demand and inflation; and both prefer shifts in interest rates to be gradual and well-signalled.

Neither man believes the central bank should be in the business of puncturing asset-price bubbles. Mr Bernanke, if anything, is more committed to this view than Mr Greenspan. At the height of the stockmarket bubble in 1999, he co-authored an influential paper with Mark Gertler of New York University which argued that central banks should focus on asset prices only insofar as they are likely to influence consumer prices. Targeting asset prices directly, his paper claimed, would create more, not less, instability. This suggests that a Bernanke Fed might be even less inclined to fret about soaring house prices than Mr Greenspan, who has only recently worried aloud about them.

Mr Bernanke will be more than just a safe pair of hands. He comes to the job with a series of big ideas about monetary policy and scant fear of stating them. At the Fed, he quickly earned a reputation as its resident intellectual, attracting attention with unconventional ideas on how to beat deflation, the benefits of inflation targeting and the idea of a global saving glut.

This willingness to question conventional wisdom is also Greenspanesque. The maestro, after all, heralded America's 1990s productivity boom long before anyone else. The difference is that Mr Greenspan couched his big ideas in caveats and conspicuous vagueness, while Mr Bernanke speaks in plain English.

That has advantages. Everyone knows that Mr Bernanke, unlike Mr Greenspan, is a long-standing supporter of the idea that the Fed should set a public target for inflation against which it can be held accountable, as many central banks do. He has written a book and endless papers advocating the practice.

Mr Bernanke will doubtless nudge the Fed towards inflation-targeting. But the change is likely to be evolutionary rather than radical. The central bank has already moved in his direction. It has become more transparent, releasing minutes of Fed meetings speedily as well as publishing two-year economic forecasts. While there is no explicit inflation target, the Fed's “comfort zone”—of core inflation between 1% and 2%—comes pretty close to one. Equally, Mr Bernanke has become less dogmatic, and he is unlikely to go on an inflation-targeting crusade.

His initial task will be to prove his inflation-fighting credentials and shake off a lingering reputation for dovishness. Soon after Mr Bernanke went to the Fed in 2002, America saw a brief deflationary scare as the economy remained sluggish while core inflation kept falling. More than any other central banker, he made clear that the Fed had “non-traditional” tools to forestall deflation, such as buying long-term bonds or, metaphorically, throwing money from helicopters. The idea of “Helicopter Ben” stuck with traders, and with it the notion that he might be just a little softer on inflation than his predecessor.

Another big Bernanke idea that is widely misinterpreted is his contention that America's current-account deficit is caused by a global saving glut rather than by profligacy at home. His thesis was

more subtle than the sound-bite suggests, but he is now seen by some as a bit nonchalant about the scale and cause of America's external imbalances. If the dollar were to crash on his watch, that reputation would not help to calm markets.

The truth is that big ideas and a stellar academic résumé are not always hallmarks of a good central banker. Arthur Burns, the only other academic to lead the Federal Reserve, in the 1970s, was a big thinker but a weak inflation-fighter. Good central bankers need technical competence, political smarts and sound judgment. Mr Bernanke has the technical competence and seems to have the political smarts (after all, he got the job). The big bet, therefore, is on his judgment.

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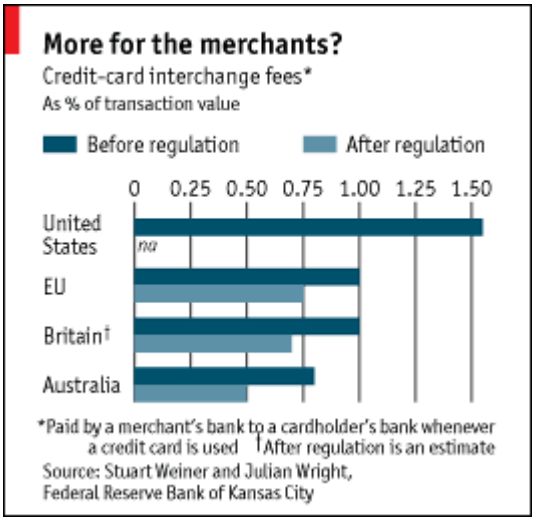
Economist.com FINANCE & ECONOMICS

Credit cards

All change

Oct 27th 2005
From The Economist print edition

Lucrative credit-card revenue is under threat



ISSUERS of credit cards are unpopular everywhere these days, and Britain's are no exception. Banks are grimly hanging on to £1.5 billion ($2.7 billion) in annual revenue that will be cut dramatically if the British consumer watchdog forces the world's two biggest credit-card associations and their bank members to reduce controversial charges. The so-called "interchange" fees account for around 15% of credit-card income in Britain, according to Mercer Oliver Wyman, a consultancy, a big whack for an industry that is struggling to keep profit margins steady.

The fees work as follows. When a customer charges a purchase, the store asks its bank to collect from the cardholder's bank. The merchant's bank pays an interchange fee to do so, and recoups it from the store. Card associations argue that the fees, which range from around 0.5% of the transaction in Australia to more than 1.5% in America, are needed to recover the cost of operating the credit-card system.

Britain's Office of Fair Trading (OFT) begs to differ. On October 19th, it objected to fees imposed by Visa, just weeks after ruling that the agreement which sets MasterCard's British rates was anti-competitive. Its chief concern is that the fees are too high, inflating charges paid by merchants and thus the price of goods and services.

In other countries—Mexico, for one—critics have used the same argument to force interchange fees lower. Australia introduced formal rules in October 2003 that cut average interchange rates from 0.95%.

Whether prices to consumers in Australia have actually fallen since then is a moot point. Its central bank argues that fees paid by merchants to card companies dropped by A$580 million ($448 million) in the year to June 30th, and that competition will pass those savings to consumers. But card associations retort that there is no statistical proof of a fall in prices, and that retailers must be pocketing the cash instead.

Many Australians now pay lower interest rates on their credit-card balances, however, even if some charges, such as annual fees, are higher and the value of reward-scheme points has diminished. Banks now compete much more on interest rates, instead of on extra card features traditionally funded by interchange fees. They have already recovered up to 40% of their lost revenue by raising costs that are more transparent to the average person than are interchange fees.

The same pattern is evident in other places where interchange rates have fallen, often as the result of regulatory threat. A study by Stuart Weiner and Julian Wright for the Federal Reserve Bank of Kansas City suggests that in many such countries annual card fees have increased. In America, where interchange rates are rising despite repeated court actions and a $3 billion settlement between card associations and retailers in 2003, the reverse has occurred: annual fees have declined and reward schemes become more generous. Morgan Stanley, an investment bank with its own credit-card business, estimates that American banks earn $24 billion from interchange fees, a figure likely to increase by $3.5 billion by 2010.

The European Commission, for its part, has struck a deal with Visa to reduce its fees to 0.7% by 2007. But the fight over interchange fees is bound to continue. For the moment, merchants' lobby groups and consumer advocates—not always happy bedfellows—seem to have the upper hand. For what it's worth.

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Refco

Fast forward

Oct 27th 2005
From The Economist print edition

The clock ticks for new bidders

IT WAS a stunningly fast corporate meltdown, even for the white-hot world of derivatives trading. An alleged fraud by Refco's former chief executive provoked a plunge in its share price and an abrupt bankruptcy filing on October 17th. Almost as quickly, a spate of potential buyers has emerged for select pieces of what was until recently one of the world's largest futures and commodities brokers. It is now a race to put together a deal before Refco melts away.

As its customers depart en masse, assets in Refco's futures unit have fallen by more than half, to $3.4 billion, since its troubles began. This week the chief executive of the Chicago Mercantile Exchange, which regulates Refco's core futures business, called for a quick resolution. “People in the markets prefer certainty versus uncertainty,” said Craig Donohue.

Initially, it looked as if the firm's futures business, which is still operating, would be snatched up by a consortium led by J.C. Flowers & Co, a private-equity firm. But the Flowers group withdrew its $768m bid on October 24th after a federal bankruptcy judge in New York balked at one condition in it. At least six other groups have shown interest in the futures business. The highest known offer is from Interactive Brokers Group, an American broker-dealer, whose bid is worth $858m. It also says it is looking at Refco's broker-dealer arm. A second bid has come from Dubai Investment Group, owned by the Dubai government, and Yucaipa, a private-equity firm run by the billionaire Ronald Burkle.

Other groups too are nosing about. These include Man Financial, Refco's major rival and part of British-based Man Group, an investment firm; a group including Merrill Lynch, an investment bank, Warburg Pincus, a private-equity firm, and Susquehanna International, an institutional brokerage; Marathon Asset Management, an investment firm; and Apollo Management, a hedge fund. Bids are due by November 4th.

Santo Maggio, head of Refco's capital-markets unit, is reported to be co-operating with federal prosecutors. Should portions of the business be revived, it would be the biggest comeback yet for a firm that has had repeated scrapes with regulators since it was founded by a cattle trader more than 30 years ago as Ray E. Friedman & Co. That firm hit the headlines in connection with Hillary Rodham Clinton, who was accused of conflict of interest in a cattle-futures investment in 1979. Mrs Clinton was cleared of violating trading rules, but the firm was fined in connection with the case.

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Economist.com FINANCE & ECONOMICS

Italian banks

Capitalia's piazza

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A small revolution in Italian banking

EVEN his rivals admit that Matteo Arpe has done a fine job of turning around Capitalia, Italy's fourth-biggest banking group. When he became chief executive in July 2003, Capitalia, which embraces three banks—Banca di Roma, Banco di Sicilia and Bipop Carire—was nearly insolvent. Having eased the bank's huge burden of dud loans, slashed operating costs and cut exposure to financial risk, Mr Arpe reported healthy profits for his bank for the first half of this year.

With the heavy restructuring work done, he is now seeking to increase revenue by getting more customers through the door. For a start, the door is to be open more often. Since October 17th, some Capitalia branches have been open at lunchtime and they are beginning to be open on Saturday too.That is hardly worth noting in many other countries, but it is something of a revolution in Italy. Customers are greeted by an employee who points them in the right direction—again, quite a departure for Italians.

The real change, though, is what takes place inside the branch. Since October 24th, a host of third-party partners are supposed to be providing non-banking services. Lottomatica, the lottery operator, is to help with payments of fines, television-licence fees, road taxes, utility bills and other transactions. The national pension association is to sort out pensioners' problems and fiscal advisers are to help with taxes. Notaries provide signature-authentication and other services. Chambers of commerce are on hand to assist small entrepreneurs with daunting paperwork. And the Fondazione Umberto Veronesi, a not-for-profit foundation for scientific research, is advising on health matters.

The idea sounds less like a traditional bank branch than a piazza buzzing with activity in the centre of town. But so far the dream is outstripping reality, at least in some branches. Business was slow earlier this week in Banca di Roma's large branch in Piazza Edison, next to the central bank's offices in Milan, Italy's financial capital. The new project has brought no changes to the layout, just a different use of two desks near the entrance.

A few hundred metres away, behind the La Scala opera house in Bipop's main Milanese branch, the touted “totem” touch-screen self-service point had not yet arrived. But a polite young lady was glad to explain the services that Capitalia now offers. The branch's digital clock was an hour slow but due to be fixed.

Across the road at Banca Intesa's imposing building, another polite young lady also stood at a help-desk, doing the job she has done since her bank introduced it a year ago. Banca Intesa is open all day until 4.15pm; a notice at Bipop's entrance said that the bank shut at 4pm and was closed between 1.20pm and 2.30pm.

One problem for Capitalia is winning over a public sceptical about banks and banking in the wake of a series of scandals at firms such as Parmalat, a dairy group, and turned off by high charges and inefficiency. Another is the fact that many of Capitalia's new services are available elsewhere.

People have paid utilities bills by direct debit for years. They can take care of road taxes and television licences at their local tobacconists, which are a lot thicker on the ground than Capitalia branches. Help with income taxes is easily available at fiscal assistance centres. The state pensions body has smartened up its act so that visiting its offices is no longer as frustrating as it was. In any case, in Milan the pensions body has not yet got fully behind the Capitalia project. And that is another problem for the bank: results will depend on the efforts and ability of outsiders.

Will it work? Quite possibly. Italians are used to buying non-banking services at bank branches. More than two-thirds of life-insurance policies are sold through banks, as are half of all mutual funds. And the venture does not need to be overwhelmingly successful to pay its way. Capitalia's revenues would rise by twice the cost of the new initiative if the rate at which clients are lost could be cut by half.

Against that, the bank-as-forum, or rough approximations of it, has had mixed success elsewhere. America's Washington Mutual has done itself no harm by selling coffee and what-not in its branches. Combining branches with a chain of coffee shops, on the other hand, did little for Britain's Abbey National (now plain Abbey).

Mr Arpe modelled his new plan on the bank with the most aggressive retail strategy either side of the Atlantic: Commerce Bank, a successful American bank set up in 1973. Its founder, Vernon Hill, prides his bank on having the lowest deposit rates and the fastest deposit growth in the market, thanks to providing an enjoyable and efficient “customer experience”. But perhaps this sort of one-stop-shopping plays better across the water.

Why visit your bank to learn which hospitals treat different types of cancer? asks an executive of a medium-sized northern Italian bank. “If I want ham, I go to the grocer's, not a pharmacy.” The head of a Milanese public-relations firm also questions the approach. “Going to an Italian bank is like going to the dentist: best avoided, but painful if unavoidable.” And a taxi-driver in Milan thinks that banks should stick to banking, at which, in any case, they are not very good. If he were to visit a local branch of Capitalia hoping to buy tickets for La Scala at the self-service point, he would find all sorts of music on in Rome but nothing at all in Milan.

Yet times are changing, even in Italy. “The idea is flawless, all depends on execution,” says Davide Serra, who analyses European banks at Morgan Stanley. According to Mr Arpe, there has been no innovation in Italian retail banking in the past 50 years. He is right. But he may find achieving this now more difficult than he found curbing Capitalia's bad debts.

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Economist.com FINANCE & ECONOMICS

Indonesian banks

The window slams shut

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Why privatisations are slowing

FOR three years, the Indonesian government has been selling stakes in the many banks it took over during the Asian crisis of 1997. As recently as September, it auctioned off 5% of Bank Central Asia, the country's second largest, for $219m. But that might be the last sale for a while, the authorities say, even though three of the country's four biggest banks remain under state control. The government simply would not make enough money from any further divestment, the minister in charge of state-owned firms explains. Local banks are beginning to lose their allure.

A year ago, the government sold a majority share in mid-sized Bank Permata to a consortium led by Standard Chartered Bank for $305m—over three times book value, and the highest price it had received for any banking asset. The appeal was simple: the economy, South-East Asia's largest, was growing at its fastest pace since the crisis, and loans were growing with it. Spreads between commercial banks' borrowing and lending rates were at record highs, even though interest rates in general were at record lows. To top it all, a new president, pledged to improve the investment climate, was about to take office.

But the government, beset by crises such as last year's tsunami, has not got around to many of its promised reforms. Economic growth has slowed. Earlier this year, real interest rates briefly turned negative and the rupiah slid. Expensive oil imports made things worse. That alarmed Bank Indonesia, the central bank, which has raised rates by 2.25 percentage points since August. The World Bank now reckons that inflation, which was 7% at the beginning of the year, might reach 14%.

All this will weigh on Indonesia's banks. Loan growth—27% last year—is slowing. Margins are declining, as banks absorb some of the rate rises rather than passing them on to precarious borrowers.

Bank Indonesia insists that local banks are in much better shape than they were seven years ago. For one thing, they are profitable and well capitalised. Foreigners have bought a number of them, reducing the risk of imprudent loans to big shareholders or their golfing buddies. Lending has diversified too, with more going to consumers and small businesses.

What's more, the central bank is regulating more aggressively. Last year, it closed two small banks. Earlier this year, it enforced stricter loan classifications, prompting Bank Mandiri and Bank Nasional Indonesia (BNI), the country's biggest and third-biggest banks respectively, to report a surge in non-performing loans.

It is no coincidence, analysts say, that both are controlled by the state, which has reformed less than private owners. It is also accused of having funnelled funds in the past to political parties, supportive tycoons and other dubious causes. This year, the state audit agency uncovered $105m of suspect loans at Bank Mandiri; its president was fired and now faces criminal charges. Prosecutors also launched two probes into fraudulent lending at BNI, which was similarly

embarrassed in 2003.

Bank Indonesia is keen to see consolidation reduce the country's 130-odd banks to 15. In a bid to improve management, it will let only the best-run banks launch takeovers. It has also lifted its blanket guarantee on deposits, which should encourage bigger customers to switch to the most reliable outfits. But the most efficient way to reform these state-owned giants would be to privatise them—and that the government is reluctant to do for now.

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Economist.com FINANCE & ECONOMICS

Fishy economics

When lobster was fertiliser

Oct 27th 2005
From The Economist print edition

What old restaurant menus say about the exploitation of the deep seas

GLENN JONES, of Texas A&M University, is a palaeo-oceanographer—an archaeologist of the oceans. He investigates both the mysteries of the deep and the secrets of the past. He and a colleague once estimated the temperature of the sea floor a century ago by studying the "isotopic composition" of mollusc shells. His latest method of inquiry, on show this week at the "Oceans Past" conference in Kolding, Denmark, is a little easier to understand. He reads old seafood menus. Lots of them. Mr Jones reckons he and his team have trawled through 40,000 or so, dating back as far as the 1850s.

Why? His menus, mostly from American cities on either coast, have allowed him to track the price of seafood back 150 years, much further than anyone has gone before. The menus show that the bountiful seas of centuries past have become more miserly in recent decades. From the early 1920s to the late 1930s, for example, a San Francisco restaurant would charge only $6-7, in today's money, for a serving of abalone, a type of mollusc. By the 1980s, however, abalone was selling for $30-40 a meal. The collapse of abalone stocks prompted a 1997 ban on commercial harvesting off California's coast.

As local waters are exhausted, restaurants buy their seafood from further afield. And as one species thins out, it falls off the menu to be replaced by another. Swordfish, for example, made its debut in American restaurants in 1909, according to Mr Jones's menus. The cost of a meal, about $7 from the 1920s to the 1950s, rose to $30-35 by the late 1970s. But these high prices tempted new suppliers from Australia and the south Atlantic, who have helped to bring the price back down.

Of course, restaurant prices reflect much more than the cost of the food on the plate: rent, for example, might also outpace inflation. But Mr Jones says that his menu prices track wholesale prices quite closely in the 50 years for which we have reliable numbers. This gives him confidence that the menus are also a sound guide to the price of a catch in the hundred years before that.

More fundamentally, a price does not reveal anything about supply, unless you also know something about demand. And Mr Jones has some interesting observations about that side of the market too. Demand for lobsters, for example, has evolved in a curious way. The armour-plated delicacy used to be super-abundant and dirt cheap, he says—so cheap that it was fed to inmates in prison and children in orphanages. Farmers even fertilised their fields with it, and servants would bargain with their employers to be given it no more than twice or thrice a week.

As the crustaceans became harder to find, canned lobster ceased to be profitable. Live lobsters, by contrast, grew in status as they became dearer. A meal that cost $4 (in today's money) in the 1870s cost $30 or more a century later. What was once a manure substitute is now a prized delicacy. What the lowliest servant once refused, the swankiest restaurateur now offers with pride. Mr Jones's menus may reveal something about the historical fate of fish, crustaceans and molluscs. But there is no accounting for that peculiar land-based mammal that eats them.

Economist.com FINANCE & ECONOMICS

Economics focus

Closing the growth gap

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From The Economist print edition

A theory to explain why Europe has fallen behind America, and how it might catch up

IN THE past ten years, the economies of what is now the euro area have grown by around 2% a year. America has managed a full percentage point more. Lots of reasonable explanations of the gap are on offer: America has freer markets than Europe; it is better at finding and using new technology; its fiscal and monetary policies have been more supportive of growth; and so forth.

You might expect such explanations, and a bundle of policy recommendations, to tumble out of theories of growth—the branch of economics concerned with the medium- and long-term fortunes of economies. You'd be disappointed. Growth theory is good at explaining why rich countries are rich and poor ones poor, but much less so at divining why some rich countries (eg, America) grow faster than others (eg, much of Europe) and telling the laggards how to catch up.

A recent paper* by Philippe Aghion, of Harvard University, and Peter Howitt, of Brown University, attempts to fill the spaces between fact, theory and policy. One branch of theory emphasises the role of capital accumulation in generating growth: save more, is the implication. This might help to explain why, say, East Asia sped past Latin America in the last part of the 20th century, but not why Europe has been trailing America: Europe, after all, has a higher saving rate. Another line of thought holds that good "institutions"—the rule of law and all that—are essential. This can account for much of the chasm between rich and poor, but not the fine variations among rich countries with sound legal and political systems. A third angle identifies innovation as the fuel for economic advance. Messrs Aghion and Howitt argue that models of this type have hitherto had little to say about how economic laggards catch up and then keep up (or not) with the latest technology—and thus about why Europe, having grown faster than America for 30 years after the second world war, stopped closing the gap and fell farther behind.

Technological advance, though, is at the core of their own approach. In essence, a given industry in a given country can use either the best technology available or an older, less efficient version. In countries already at the cutting edge, innovation is the source of growth. Those not at the frontier advance by implementing existing, but still better, methods of production.

From this, two observations follow. The first is that the institutions and policies best suited to countries at the leading edge need not be the right ones in less advanced places. Education, say Messrs Aghion and Howitt, is a case in point. The closer a country is to the technological frontier, the more growth depends on having a highly educated workforce. Further back from the frontier, education still matters; but university degrees matter relatively less and good primary and secondary education count for relatively more. Evidence from different countries and from American states appears to bear this out. And what does this imply for the transatlantic growth gap? America spends around 3% of its GDP on tertiary education; the European Union only 1.4%. More than a third of Americans have degrees; fewer than a quarter of Europeans do. Against that, many EU countries are considered to have stronger secondary education than America does. Europe may therefore have been well equipped for its post-war decades of chasing the United

States, but did not adopt the policies needed to push back the technological limits.

The second observation is that, whereas most theories of growth laud the accumulation of capital, it is sometimes good to see it destroyed. Growth is likely to be higher if markets are open to new entrants, which either drive less efficient incumbents out of business or scare others into investing, updating their technology and seeing off the raiders. Again, this is likely to matter more the closer countries are to the limits of technology. And again, the destructive process appears to have a freer rein in America than in Europe. For example, say the authors, half of all America's new pharmaceutical products are introduced by firms less than ten years old; the proportion in the EU is only 10%.

Budgeting for growth

More controversially, Messrs Aghion and Howitt also turn their attention to macroeconomic policy. Most economists think that budgets and interest rates ought to be geared mainly to the short-run course of the economy. Not necessarily so, say the authors: countercyclical budgetary policy can be aimed at long-term growth, and the case is stronger in Europe than in America.

If capital markets are well developed, they argue, sound companies can borrow to tide them over in recessions; if those markets are thin, good businesses will sink. And where capital markets are less well-developed, policies that dampen the business cycle can help more good firms to survive. Econometric tests suggest that well-targeted fiscal policy—investment, rather than government consumption—might work. Because Europe's capital markets are less deep than America's (its ratio of private credit to GDP, for example, is much lower), budgetary policy ought to lean against the cycle more in Europe than in America. In recent years, however, the opposite has been true.

When Mr Aghion proposed this idea last month, at the annual conference of the Centre for Economic Policy Research and the European Summer Institute in Frankfurt, he met a fair bit of scepticism. It is easy to see why. Countercyclical policy is much harder to get right on purpose than by accident. And, as one economist there remarked, America's growth rate has actually been more volatile than Europe's—implying that Europe has less need to smooth out cycles to encourage growth. Still, Mr Aghion and Mr Howitt have produced some provocative research. More—and more arguments—will surely follow.

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* “Appropriate Growth Policy: A Unifying Framework.” Available at post.economics.harvard.edu/faculty/aghion/papers/Appropriate_Growth.pdf

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Economist.com SCIENCE & TECHNOLOGY

Human genetics

Finding needles in a haystack

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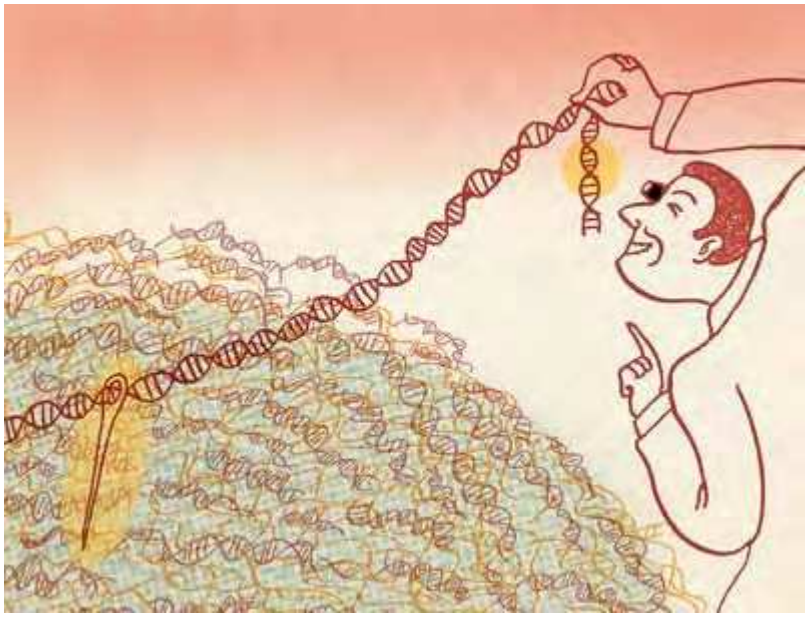

A new map will accelerate the discovery of genes that cause disease

Get article background

ALL people are 99.9% alike, genetically speaking. That is to say, the DNA sequences of two unrelated people are 99.9% identical. It is the remaining tiny fraction of a percentage point that accounts for how people differ from each other. This includes how one person might be more prone to disease and how another might respond differently to treatment. Understanding these differences thus offers scientists the opportunity to understand and, potentially, treat complex diseases such as asthma, diabetes, high blood pressure, heart disease, obesity and even cancer.

An international team of researchers has now announced a big step towards achieving such goals. It has published the results of a three-year effort to chart the patterns of the most frequently occurring genetic differences in the world's population. The findings mean that the search for clinically relevant genes can be accelerated through the use of a clever short cut.

The human genome consists of about 3 billion base pairs (the chemical “letters” of which DNA is composed). Only a small fraction of these form 30,000 genes; the rest is thought to be junk. Each gene consists of a length of DNA that contains an instruction to do something. The command is usually to build the proteins that do the donkeywork of maintaining life, although some genes control how much protein to produce and when.

How people vary in their susceptibility to disease and their response to treatment is linked to

places in the genome where the DNA sequence varies. Much genetic variation is caused by changes in single letters, or bases, called single nucleotide polymorphisms. As a result, every individual has a unique genetic code that typically differs in about 3m nucleotides from everybody else's. Like the rest of the genome, these small variations are inherited. Thus, in large societies, many individuals can carry the rarer version of the single letter variation in their DNA sequence.

Researchers trying to discover the genes that make some people susceptible to certain diseases compare a group of sick people with a group of healthy ones. This is like looking for the proverbial needle in a haystack—there are 10m different single-letter variations in societies where 1% or more of the population has the rarer form.

A cunning plan

The researchers, led by David Altshuler of Massachusetts General Hospital in Boston and Peter Donnelly of the University of Oxford in Britain, wanted to find a quicker way. Single-letter variations that are close together in the chromosome tend to be inherited as intact blocks of information. By putting these single-letter variations in the human genome into groups, called haplotypes, the team hoped to do the equivalent of identifying entire neighbourhoods by examining just a few of the houses on each of its streets.

Most of the common haplotypes occur in all human populations. However, their frequencies differ between ethnic groups. The researchers focused on four populations that were known to be sufficiently different to represent much of humanity when added together. The samples came from Yoruba in Ibadan, Nigeria; Japanese in Tokyo; Han Chinese in Beijing; and Utah residents with ancestry from northern and western Europe.

The researchers measured these variations in the DNA found in blood samples from 269 individuals living in these four societies. Specifically, they compared 1m of the single-letter differences to produce what is dubbed the “HapMap”. The map, published in the current issue of *Nature*, confirms that it is indeed possible to rely on a relatively small number of single-letter variations to see the bigger picture. It identifies the 250,000 to 500,000 single-letter variations that provide almost as much mapping information as all 10m single-letter variations. Thus, the researchers hope it will make searching the human genome for hereditary factors common in disease up to 20 times faster.

Quickly identifying which people are at risk of disease could be beneficial in itself. If, for example, the 10 to 20 genetic markers that predispose people to colon cancer were to be identified, individuals who had those genes could be kept under closer observation. That way, tumours could be removed when they were still small. At this stage, the cancer is 95% curable. Faster identification of genetic disease would also accelerate the development of treatments that could target disease-causing genes.

The HapMap provides researchers with indicators—Dr Donnelly likens them to Post-it notes—for focusing on genes involved in common diseases. However, like the Human Genome Project before it, the map is incomplete. The researchers have examined just 1m single-letter variations so far. They plan to take a look at a further 2m in the coming few years. Fundamentally, the study of human genomic variation can never be complete, because each person carries unique as well as common variations.

The similarities between the map of the human genome and the HapMap might not be as great as 99.9%. The race to map the human genome was between a large public consortium and a private company. HapMap is being published by publicly and privately funded scientists working collaboratively, although the information produced is freely available. What unites them is that

both maps will greatly benefit human health.

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Economist.com SCIENCE & TECHNOLOGY

Neurology

Illusions and delusions

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People with schizophrenia see more clearly by ignoring visual context

“THE patients that I have observed do not respond to situations as they should; they are frightened by what is not there, yet they remain indifferent to what is.” These words, spoken by Eugene Bleuler—the Swiss psychiatrist who coined the term “schizophrenia” in 1911—remain true today. Yet scientists have now discovered that schizophrenia sufferers can see much more clearly than people who do not have the disorder.

A team of researchers led by Steven Dakin of University College London set out to find a test in which schizophrenia sufferers would do well. Given that people with schizophrenia tend to perform poorly in any test, tasks at which they excel are both rare and revealing. The enhanced performance cannot be attributed to general factors and serves to illuminate the condition's underlying neural mechanism.

The researchers showed two groups of people a visual illusion. One group was suffering from chronic schizophrenia and the other not. The illusion consisted of a faint-looking patterned disc surrounded by an area containing a highly visible black-and-white pattern. Surrounding the first area with the second produces a visual illusion in people without schizophrenia, who think the first image is fainter than it actually is. However, people who have schizophrenia are not so easy to fool.

Of the 15 participants with chronic schizophrenia, 12 made more accurate judgments than the most accurate person in a control group of 33 non-schizophrenic volunteers. Moreover, one of the two people with schizophrenia who were less accurate than the most accurate person without schizophrenia has since been re-diagnosed as suffering from bipolar disorder. The research was published last week in *Current Biology*.

The work adds weight to the notion that people with schizophrenia cannot filter out irrelevant information and their brains are thus being overwhelmed. Given that those with schizophrenia appear to take less account of the context in which they receive visual information, this might be part of a more general failure to deal appropriately with context. It could explain why some sufferers might misattribute people's actions or feel persecuted.

The research seems to confirm the guess of Dr Bleuler, who described schizophrenia sufferers as “flooded with an undifferentiated mass of incoming sensory data”. A century on, this description accords well with the finding that contextual suppression—the neural process that quells the visual flood—is indeed weaker in those with schizophrenia. The research suggests this is due to the failure of a specific visual mechanism, rather than to general factors such as attention deficit. The next test will be to discover whether people with schizophrenia can also hear, smell, touch and taste things more accurately, but with less attention to context, than those without the disorder.

Economist.com SCIENCE & TECHNOLOGY

Satellites

Spaced-out students

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From The Economist print edition

A European satellite built entirely by students is due to be launched

URBAN myths have grown up around projects conceived and constructed by students. There is the one about the university library built atop an existing, but now sinking, building—the students had failed to account for the weight of the books. There is the one about the unused, empty swimming pool—the students had forgotten to include the weight of the water. The European Space Agency, which as *The Economist* went to press, was due to launch a satellite built entirely by students, will be hoping for a more successful outcome.

Lost in space?

The Student Space Exploration and Technology Initiative (SSETI), a programme established by the agency to boost interest in space science among European youngsters, has an ambitious agenda. The launch on October 27th of SSETI Express, a low-Earth orbit spacecraft carrying a further three minuscule satellites, is the first of any satellite to be designed by a pan-European team of students. It is expected to be followed by the European Student Earth Orbiter, scheduled for launch in 2008; and the European Student Moon Orbiter, planned for 2010-12, which will conduct experiments on its way to the moon and while in orbit around it.

Three objectives underlie the present project. The first is to carry—and subsequently deploy—three satellites that are 10-cm cubes. One of these “CubeSats” will test whether it is possible to trace the whereabouts of such a small object in space, another will explore the effects of miniaturising technology and the third is pioneering a new type of solar cell. The larger satellite will also send images back to Earth.

The second objective is to test hardware being developed for future projects. Indeed, the Earth orbiter had originally been intended as the first SSETI mission, but the complex design of some of its subsystems made the work take longer than expected. SSETI Express will thus test aspects of this proposed future spacecraft.

But the third, and perhaps the most important, objective has already been met. The project has involved more than 300 students from ten different countries, and most of the co-ordination has taken place over the internet. This has shown that complicated projects can be accomplished with only minimal face-to-face contact. Indeed, the satellite has taken just 18 months to design and build, little more than a final-year lab project.

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Economist.com SCIENCE & TECHNOLOGY

Sleep

Dreams are made of this

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Studies are shedding light on the mystery of sleep

ANYONE who has ever owned a hamster will know that the animal spends an inordinate amount of time sleeping. Depending on your point of view, that might be a good or bad thing. Hamsters are small and, broadly speaking, the smaller the animal, the more sleep it needs. While elephants need as little as three or four hours of sleep per day, tiny opossums will snooze for 18 to 20 hours. Flipper, however, doesn't seem to sleep at all—at least not in any way that humans know it. In the bottlenose dolphin, each side of the brain appears to take it in turns to do something that is equivalent to sleep but with only one eye closed.

Such animal curiosities give scientists clues to the function of sleep and thus what it is, and what it is for, in humans. It is clear that sleep is more than the absence of wakefulness—it is the reorganisation of the brain's neuronal activity. During sleep, the brain is very active and two different states, non-rapid eye movement (NREM) and rapid eye movement (REM) sleep occur. These are as different from each other as they are from wakefulness, which means humans have three very different states of being, rather than two. In each, most parts of the brain are active but in different ways.

When humans are deprived of sleep—something they spend about a third of their lives doing—they accumulate a sleep “debt”. In other words, they must ultimately make up for some of the missed sleep if they are to continue to function. Clearly, something important is happening. But when only REM sleep is suppressed, either through brain lesions or some anti-depressant drugs, there are no obvious cognitive or physiological symptoms. So these two sleep states are likely to have different purposes.

There are many theories about the function of NREM sleep, with its reduction in brain metabolic activity. One is that it may conserve energy at some times of day in the same way hibernation does during particular seasons. Another role for NREM sleep is also suggested by recent work showing that sleep may have a role in allowing, or facilitating, the growth of new neurons in adults.

Jerome Siegel, of the University of California in Los Angeles, along with colleagues elsewhere, has suggested a third possibility. Writing in a special review of sleep in the current issue of *Nature*, Dr Siegel says that it may be related to defence against oxidative stress. Smaller animals have higher metabolic rates, and this results in the generation of higher levels of small, highly reactive molecules such as free radicals. Studies on rats show that when they are deprived of sleep, their oxidative stress increases. Dr Siegel proposes that animals with higher metabolic rates need more sleep to interrupt and protect against this kind of oxidative damage, as well as repairing any damage done.

Sleeping on it

REM sleep, which accounts for 20% of human sleep, is different from NREM sleep because the brain's metabolic activity remains high, as does its neuronal activity. Eyes and extremities twitch, and this is the point where humans are most likely to have illogical or bizarre thoughts, and vivid dreams—such as being eaten by an enormous snake.

One popular theory is that it is required for the consolidation of memories. The obvious flaw in this suggestion is that one does not have to have been eaten by an Anaconda or sat a maths exam naked in order to have this kind of dream. Indeed, recent studies suggest that only 1.4% of dream reports portray complete experienced memories. Typically fragments of memories are most common, although complete memories are more likely to be dreamed about after a traumatic experience. In one study, 65% of dream elements were linked to features of waking events. Such research, though, is difficult to do because it is based on subjective reports.

It seems likely that sleep is an important component of how memories are formed and shaped. Dreaming about newly learned material enhances its subsequent recall. However, the exact relationship between dreams and memory remains enigmatic. There is clearly more at work than the replaying of memories during sleep. Robert Stickgold of the Harvard Medical School thinks that memories are not being reactivated at all because brain-imaging studies show an area of the brain involved in memory recall is deactivated in sleep, especially REM sleep.

Allan Hobson, also of the Harvard Medical School, says that research suggests REM sleep is a physiological brain state that produces a distinctive and psychosis-like mental content, in which the sleeping brain can either generate its own perceptions or think about them, but it cannot do both.

However, dreams do simulate reality in several intriguing ways. One could be eaten by a snake in an exact replica of one's bathroom—that is, in a real, spatially coherent environment. And it also might be possible to have a discussion with the snake's owner, or experience the sensation of being swallowed, while maintaining a steady stream of perception throughout the whole dream. Such matters science is still struggling to understand. What exactly is the hamster dreaming during all those hours it spends asleep? That is one question that even science may never be able to answer.

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Economist.com BOOKS & ARTS

Design

Foiling fear

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In design, as in other areas, terror is a great motivator

Cameron McNall

FEAR may always be with us, but the objects of it change with time. Victorian anxieties about premature burial produced a flurry of 19th-century patents for “safety coffins” with breathing tubes and with connecting rods that could raise a flag or ring a bell above ground. Now our worries include AIDS and avian flu, heart attacks and homelessness. These are the enemies against which modern designers and engineers seek to pit their skills, producing new deterrents and defences ranging from bandages to bollards, which aim to combine effectiveness with ease of use.

“SAFE: Design Takes On Risk”, a new show at the Museum of Modern Art, looks at how designers rise to the challenge. It has assembled 300 products and prototypes meant to protect human beings (and, in a few cases, animals and plants) against perceived current dangers.

The objects range from a bullet-proof T-shirt to a tracheotomy kit that fits on a key-ring, by way of a hard-hat for small animals and a bedside table which disassembles into a hefty wooden club and shield. Big fears get equal space with small, even trivial, ones. The aim is to capture a “gamut of fears from the paper-cut to genocide, presented without any kind of judgment,” says Paola Antonelli, the museum's curator of architecture and design. A computerised command centre for city-wide crisis management jostles with a white-noise generator placed in Japanese lavatories to spare users the fear that their ablutions might be overheard.

This is the first major design exhibition at MoMA since the museum returned almost a year ago from a temporary home in Queens to the much-enlarged main building on West 53rd Street in

Manhattan. It looks, on the face of it, as if MoMA were paying straightforward homage to the terrorist attacks of September 11th 2001. But, as Ms Antonelli explains, the story is a bit more complicated.

In March 2001 she had proposed an exhibition called “Emergency”, devoted to emergency-response equipment and tools. Preparation for that show was under way when September 11th intervened, with an emergency that was far vaster than anything MoMA could have imagined, and the idea was shelved. During the time that MoMA was displaced to Queens, from May 2002 until November 2004, the exhibition was re-imagined around a broader and intellectually richer theme—not of emergency in particular, but of safety in general.

Almost by definition, many of the objects here—especially those related to survival and rescue—are an exacting test of any designer's skills. They must work well in the least forgiving of conditions, and with distracted or incapacitated users. They will tend to aim for the purest possible marriage of form and function, leaving zero scope for confusion and misuse. And they may often need to be very cheap, to reach those in need. The result is that the most striking products can often be the most basic ones: a blow-up plastic shelter for a street-sleeper which costs about $5 to make and can be inflated and heated free of charge from the ventilation duct of any nearby building (see picture).

Ms Antonelli intends the message to be one of qualified optimism. She wants her visitors to leave, not so much depressed by the sheer scale of the dangers which surround them, as encouraged by the intelligence and the ingenuity with which those threats can be countered. And to lift the mood further, she has seeded the sometimes grim displays of surgical and survivalist paraphernalia with ironic pieces of offbeat design and conceptual art, including furniture you can hide in, an armoured duvet and razor-wire cut in the shape of butterflies and fish.

You would need an exaggerated degree of fearfulness to see a place for all of these things in your life. But exactly that condition has been gaining ground in American life since September 11th. Anywhere else, a collection of objects like this would seem a touch arbitrary. Here, it has the spirit of its time and place.

“SAFE: Design Takes On Risk” is at the Museum of Modern Art, New York, until January 2nd. See also our review of MoMA itself and of its restaurant

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Economist.com BOOKS & ARTS

Muslims in Europe

Confusing and confused

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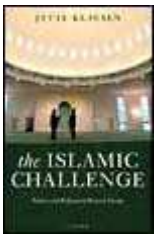
A DANISH supermarket fires a cashier for wearing a headscarf on the grounds that it might get stuck in the till. The German state of Baden-Württemberg prohibits the wearing of the headscarf by teachers, but not students. France bans the garment altogether from state schools, citing Article 9 of the European Convention on Human Rights. A British court cites the same article to uphold a schoolgirl's right to wear the much bulkier covering known as a *jilbab*.

The Islamic Challenge: Politics and Religion in Western Europe
By Jytte Klausen



Oxford University Press; 264 pages; £18.99. To be published in America by Oxford University Press in December

Buy it at
Amazon.com
Amazon.co.uk

Welcome to the confused and confusing world of European Islam. One of the main themes of Jytte Klausen's refreshingly down-to-earth book is that western Europeans have got themselves into a terrible muddle over the 15 million-or-so Muslims in their midst. (One of the many gaps in our knowledge is how many there actually are.) She coolly dismisses the view of Samuel Huntington—the Harvard professor who fathered the "clash of civilisations" thesis—that Muslims in the West are an "indigestible minority". As for the view, expressed by a Catholic bishop, that a wave of petrodollars is funding a Muslim "reconquest" of Europe, she sees this as alarmist nonsense.

Ms Klausen, a professor of politics at Brandeis University, has interviewed about 300 Muslims in six countries: Sweden, Denmark and the Netherlands, Britain, France and Germany. This elite of councillors, lawyers, engineers and doctors may hold the key to successful Muslim integration. Although her sample includes a few Islamist activists and religious conservatives, Ms Klausen sees the majority as being "overwhelmingly secular in outlook and supportive of core liberal values". In other words, they do not conform in the slightest to the popular stereotype.

She acknowledges (how could she not?) that the Madrid and London bombings have given added urgency to the questions raised by the presence of these new Muslim communities. But she insists that terrorism and security are incidental to the main issues which often bring Muslim and non-Muslim into contention. Burying the dead, training imams, provision of *halal* meat, even translating the Koran into, say, Swedish: mundane though they may be, these are among the pressing day-to-day concerns that societies and governments and legal systems need to face; and, Ms Klausen argues, are not facing.

While hostile to resurgent xenophobic parties across the continent, and insistent that European leaders must do more to bear what she calls the "burden of adjustment", Ms Klausen is unwilling to let Muslims themselves off the hook. Muslim elites which, rightly, insist on equality before the law need to confront questions they would rather duck, including gay rights, polygamy and the often fuzzy line between arranged and forced marriage.

This valuable book may also force Europeans to question the self-image of their continent as an

essentially secular place. Church pews may be empty, but religion, and the politics of religion, are now an inescapable part of the public agenda.

The Islamic Challenge: Politics and Religion in Western Europe.
By Jytte Klausen.
Oxford University Press; 264 pages; £18.99. To be published in America by Oxford University Press in December

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Nazi Germany

They stooped to conquer

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HISTORIES of Hitler get bigger all the time. Five years ago, Sir Ian Kershaw concluded his monumental two-volume life of the German dictator. Now, Richard Evans, professor of modern history at Cambridge University, is bringing out a three-volume study of the Third Reich and its origins. The escalating size of these histories is easily explained. There is more secondary literature on Hitler and the Nazis than could possibly be read in a lifetime, while historians have moved away from offering simplistic explanations for what happened in Germany in the middle of the 20th century.

The Third Reich in Power: 1933-1939
By Richard J. Evans

Penguin Press; 941 pages; $37.95.
Penguin/Allen Lane; £30

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In the 1960s, Hitler, and fascism in general, were dismissed by Marxist historians as capitalism's panic-driven response to the inter-war economic and social crisis. Other historians focused on Hitler's personal history as if this were emblematic of the wider story. The German people were seen as prisoners of his madness; mere victims. Now the big questions are different. The reality is immensely complex. There are many causes, not one.

This is the thrust of Mr Evans's argument in the second volume of his trilogy. Dictatorships are ultimately based on terror—not necessarily overt repression, but the knowledge that lurks at the back of every citizen's mind that there are lines that cannot be crossed without incurring terrible penalties. These are not necessarily conventional lines established by an easily recognised social morality. Second-guessing what National Socialism might regard as a political crime was a risky business. Silence was preferred; the averted gaze replaced the straight stare. Only a very few brave Germans tried to keep other political options alive, often earning a spell in a camp for their pains. News of how awful the camp experience was rippled out from the families who had suffered, resulting in an efficient, private compliance.

Germans prided themselves on their respectability, which was why they hesitated to confront the illegal Nazi regime, or simply argued to themselves that the dictatorship was a necessary stabiliser. Mr Evans has interesting things to say about how few qualms party bosses (and minor functionaries) seemed to have about not being respectable in the old-fashioned bourgeois sense. They lined their pockets, stole Jewish property and helped each other along. The sense that the dictatorship was utterly corrupting of conventional morality has been fiercely debated, especially since April, when Götz Aly, a visiting historian at Frankfurt University, published his “Hitlers Voltsstaat” (Fischer), about the wholesale robbery in which Germans were engaged during the war.

Mr Evans writes about the regime's efforts to remould the German mentality, but he suggests that long-established Christian conventions were hard to break down. The dictatorship worked best in areas where the peculiarities of German Christianity matched the prejudices of the new system—in penalising, for example, social “outsiders” of all kinds, from homosexuals to gypsies. He also

makes a great deal of the race question, and shows that this was by no means only about Jews. The 1930s were filled with efforts to purify the race, encourage a high birth rate among the most "Aryan" in the ethnic German population and stamp hard on anything that smacked of race defilement, including abortion, prostitution and homosexuality.

There were grim ironies in all this. The 115,000 married SS men, who were chosen for their racial characteristics and subjected to pompous propaganda on the child-rich life, could manage only an average of 1.1 children per household. The gap between racial utopia and the muddled biological reality of the German population eventually supplied one of the most damaging and long-lasting legacies of the system. Millions of Germans could come to terms with life after dictatorship in 1945, but the 300,000 men and women compulsorily sterilised were scarred for life.

Mr Evans has produced a rich and detailed description of just what the Third Reich did in every compartment of the state and every corner of society. He does not follow the fashionable view that Hitler was a weak dictator, who was unable to rein in the growing radicalisation of the system and with little interest in the routines of governing. Indeed, he concludes his vast survey by reminding the reader that Hitler was always "in the driving seat, determining the general direction in which things moved". This interpretation seems irrefutable in the face of the evidence. Hitler is there at the heart of major affairs of state, which he viewed as the work of a messianic leader.

Mr Evans's writing is a model of clarity and intelligence, but there are a few areas where the book is less sure-footed. The treatment of foreign policy, from the occupation of the Rhineland to the outbreak of war in 1939, leaves out much that is needed to understand the eventual outcome. The complicated stories about economic revival and military expansion would benefit from the occasional chart of statistics. The economic issues are described, but not explained in any great detail. Hitler's financial "wizard", a banker named Hjalmar Schacht, is given the credit for rescuing Germany's finances, but there is no economic analysis of how he did this.

These are not key areas for Mr Evans. The text comes most to life when he is talking about society, culture and politics. One final concern: many German titles have been translated into English. While it might work to cast "Mein Kampf" as "My Struggle", some other terms will seem more exotic in English than in German. For example, Julius Streicher's rabidly anti-Semitic paper "Der Stürmer" is translated as the "Stormer", although this term is never used in the English-language literature on the Third Reich. It would be like insisting that *The Economist* should be *Der Volkswirt* when it is cited in Germany. But this is a minor quibble. Mr Evans's magisterial study should be on our shelves for a long time to come.

The Third Reich in Power: 1933-1939
By Richard J. Evans
Penguin Press; 941 pages; $37.95.
Penguin/Allen Lane; £30

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American democracy

The people's road

Oct 27th 2005
From The Economist print edition

Achieving democracy in early America was a long, slow haul

Achieving democracy in early America was a long, slow haul

DEMOCRACY is a word that gets bandied about. George Bush likes to remind voters of the pressing need to “secure freedom and democracy” in Iraq. Afghanistan's recent elections signal that it is on the “road toward a stable democracy”. The United Nations has lately (at America's urging) started up a “Democracy Fund” as a bulwark for fragile democracies. And so it goes.

Yet democracy is a fluid concept. No one knows this better than the world's oldest continuous democracy. Minority rights, which Mr Bush says are among the “common principles” of democracies, were non-existent when America began. Its founders held slaves. They excluded blacks, women and many landless white men from voting. Free speech was often elusive, and even the much-feted system of checks and balances got off to a rocky start as early presidents simply ignored Supreme Court rulings.

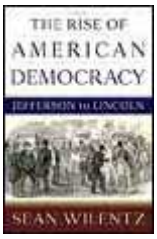
In a new book, Sean Wilentz, a history professor at Princeton University, contends that despite some promising principles, at the outset “the republic was not democratic”. Nor did those in power wish it to be. Thomas Jefferson was in a distinct minority when he declared, “I am not among those who fear the people. They, and not the rich, are our dependence for continued freedom.” Jefferson's planter friends regarded democracy as a blind alley: in Mr Wilentz's phrasing, it was dangerous to hand power to the “impassioned, unenlightened masses”.

When reform came, it was a halting process, and largely the result of the new economic and social realities of the expanding republic. The profusion of religions also played a role, as did the aggressiveness of party organisations. Mr Wilentz gets incensed by Federalist “mossbacks”, who despaired at the extension of voting rights to landless whites in the early 19th century.

This is a dense, authoritative and well-written study. It has been ten years in the making, and brings together an impressive accrual of detail. From the Alien and Sedition Acts and the Missouri Compromise to the election of Abraham Lincoln, every development is given careful study.

The book also contains many analytical nuggets. Why, the author asks, are not more federal officials impeached (or at least seriously threatened with impeachment), given the stark

The Rise of American Democracy: Jefferson to Lincoln
By Sean Wilentz



Norton; 992 pages; $35

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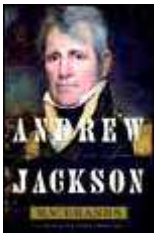
Andrew Jackson: His Life and Times
By H.W. Brands



Doubleday; 640 pages; $35

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partisanship of politics today? The answer, Mr Wilentz says, harks back to 1804-05, when Samuel Chase, a Supreme Court justice, was impeached by the House of Representatives. His misdeeds largely consisted of being a staunch Federalist and crossing President Thomas Jefferson, a Republican. But the Republican-majority Senate broke with Jefferson and voted to acquit, signalling that the standard must be greater than mere ideology. Chase remains the only Supreme Court justice ever impeached.

Much of the narrative, of course, is taken up with the slave battles. Mr Wilentz cuts through the myths—even the Missouri Compromise was not a “compromise”, he insists, owing to the way it was constructed. Some of Congress's fiercest fights were over the admission of new states to the union, and whether they should be slave or free. Often, Mr Wilentz explains, the free-staters in places like Kansas were motivated by the ignoble desire to ensure that theirs was a lily-white enclave. Mr Wilentz also shows how slaveholders kept a chokehold on local power in much of the South; one reason they feared northern abolitionist propaganda was that it might generally sow doubts about the system among landless whites as well as among slaves.

A central figure in early American democracy and the evolving north-south rows was Andrew Jackson. Orphaned during the revolutionary war, Jackson rose from nothing to prominence in the fights against the native Indians, and he later became a national hero at the end of the war of 1812. When a large British force threatened New Orleans in 1815, he trounced them, helping to strengthen America's shaky grasp on the Louisiana territory and promote westward expansion.

From there, the presidency seemed a quite obvious step. But the country had never seen a candidate like Jackson. Most early presidents were intellectuals. Jackson was the first since George Washington to be a military hero. Unlike the austere Washington, he also energetically embraced the masses, who returned the compliment by turning out to vote as never before. (Grumbled one rival, Henry Clay, “I cannot believe that killing 2,500 Englishmen at New Orleans qualifies for the various, difficult and complicated duties of the Chief Magistrate.”)

Jackson finally attained the presidency in 1829, despite the best efforts of his opponents, who took character assassination to a new level during the campaign, with slurs about his “adulteress” wife and his “prostitute” mother: another, less salubrious step in an evolving democracy.

Jackson and the democratic revolution he swept in form the basis of a new biography by H.W. Brands, a wonderful storyteller who has written eloquently on many topics including Benjamin Franklin, Texas's revolution and the California gold rush. Mr Brands's challenge is greater here, for Jackson is an ambiguous figure and the book's muscular and enthusiastic tone is sometimes a poor fit with its subject.

Commonly known as “Old Hickory”, Jackson turns out to have been on the wrong side of history on many issues. He was an unabashed slaveholder who needlessly slaughtered Indians, and even went so far as to cut out tribes who fought as his allies from land deals. His policies as president led to the “Trail of Tears”, in which tribes were forced from the lands they had obtained by treaty from the federal government. Thousands of Cherokees died on the trek from the south to Oklahoma so that whites could till the rich Georgia soil.

Jackson also instigated financial turmoil. Having lived through a period of boom-and-bust land speculation, he distrusted paper money and banks. During his second term, he vetoed the renewal of the charter for the independent Second Bank of the United States, a private institution that kept the federal government's deposits interest-free, and issued uniform paper currency. Jackson had some legitimate concerns about the bank, which he also viewed as unconstitutional—but in waging his struggle, he hurt not just the bankers, but also the ordinary citizens that Jacksonian democracy was meant to support. That Jackson's visage remains on the $20, America's second-most widely circulated bill, is both curious and ironic.

So why does the myth of Jackson persist? Besides giving voice to the common man, Jackson was above all a committed unionist, argues Mr Brands. The main crisis of his first term was South Carolina's attempt to nullify a federal law on tariffs that it did not like. This amounted to a constitutional showdown. Jackson's one-line toast at the moment of crisis—“Our Federal Union: it must be preserved”—helped to carry the day. South Carolina backed off. But, despite Mr Brands's enthusiasm for his subject, such achievements still leave Jackson, as democrat and statesman, far short of the class of Abraham Lincoln.

The Rise of American Democracy: Jefferson to Lincoln.
By Sean Wilentz.
Norton; 992 pages; $35

Andrew Jackson: His Life and Times.
By H.W. Brands.
Doubleday; 640 pages; $35

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New film

Funny man

Oct 27th 2005 | ROME
From The Economist print edition

Roberto Benigni fashions barbs from poetry

AP

There's a tiger in his tank

IN HIS autobiography, Charlie Chaplin said that, if he had known about the horrors of the concentration camps, he would never have made a film which made fun of the "homicidal insanity of the Nazis". He might have thought differently if he had seen the work of Roberto Benigni, an Italian comic actor who made farcical parables about serial killers and Mafiosi, before he too took on the Nazis in his 1997 Oscar-winning film, "La Vita è Bella" ("Life is Beautiful"). Eight years on Mr Benigni has turned his attention to Iraq.

In his new film, "La Tigre e la Neve" ("The Tiger and the Snow"), Mr Benigni is a schoolteacher named Attilio who teaches and writes poetry. The film opens with a dream: Attilio, in his underwear, is in a church about to marry a girl named Vittoria (played by Mr Benigni's usual leading lady, his wife Nicoletta Braschi). An orthodox priest is officiating, and at the piano sits the gravelly-voiced Tom Waits.

When Attilio awakes, he sets about pursuing Vittoria, who does not altogether appear to appreciate his insistence. She tells him he will only win her heart when she sees a tiger in the snow in Rome, alluding to the title of a book of poetry that Attilio has just published. Vittoria, meanwhile, is dedicating her time to writing a book of her own, about Fuad, an exiled Iraqi poet (Jean Reno), who in the wake of Saddam Hussein's fall returns to Baghdad where Vittoria soon joins him.

When Attilio hears she has been injured in a suicide bomb attack, he goes to her aid, bluffing his way into Baghdad as an Italian Red Cross helper. Discovering that Vittoria is in a coma, he becomes determined to find the medicine she needs. Against the background of a flaming Baghdad—filmed in Tunisia—the Benigni gag parade, which is better on-screen than on-page, begins to roll. He "borrows" a motorcycle, only to find it runs dry in the desert. Two camels coyly compete to give him a lift. When he arrives at an American check-point loaded with ominous looking packages (all medicines, of course), the terrified American soldiers ask him who he is. "I'm a poet," he replies, "like Dante or Walt Whitman." One of the soldiers knows who Whitman was and smilingly lets him through.

As a film-maker Mr Benigni continues to be a naïf, but weren't all the great comics? Much of the dialogue in the film is inspired by poems. The satirical message is clear, even if there are many who would never consider farce a weapon.

Correction: Agincourt

Oct 27th 2005
From The Economist print edition

Our review of Juliet Barker's book on the battle of Agincourt last week stated that a longbow weighed 150 pounds. What we should have said is that its pull-weight, or draw-weight, was 150 pounds. Even English archers were not that impressive. Sorry. This has now been corrected online.

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Obituary

Rosa Parks

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From The Economist print edition

AP

Rosa Parks, a pioneer of civil rights, died on October 24th, aged 92

AS THE bus approached, she knew this particular driver was trouble. He had turned her off once before because, after paying her fare, she had refused to walk round the bus to get in by the back door. Rosa Parks knew better than to do that. While you walked round, the driver was quite capable of shutting the doors and driving off, leaving you stranded. So she had got in at the front and walked through to the back, like anybody else.

Or not quite like anybody else. In Montgomery, Alabama in the 1950s, as in much of the South, the first four rows of seats were for whites only. No more than four rows were needed, since few whites, and those poor ones, took the bus anyway. But whether they were filled or not, no black could sit there. Blacks sat at the back, in “Coloured”, where they belonged.

Between the two worlds was a middle section. Blacks could sit there, but if a white needed their seat they were expected to vacate not one seat, but the whole row, in order to spare the white the embarrassment of sitting by a nigger. On December 1st 1955, Mrs Parks sat in that section. After three stops, a white needed a seat. The three other blacks in the row stood up meekly, but when the driver ordered Mrs Parks out, she said, firmly, “No”.

In the mythology that came to gild this scene, Mrs Parks, who was 42, was said to have complained that her feet were tired. She herself denied it. Her job, as a seamstress in a department store, did not involve much standing. What had wearied her was drinking from black-only water-fountains, using black-only elevators, going to the back, standing aside, being demeaned in a hundred ways. She wanted no more of it. On December 5th, on the day she was convicted of violating a city ordinance and behaving in a disorderly manner, the young minister of

the Dexter Street Baptist church in Montgomery, Martin Luther King, summed it up: “We are tired, tired of being segregated and humiliated, tired of being kicked about by the brutal feet of oppression.”

Mrs Parks had meant to do no more, she said, than show one rude bus-driver that blacks were being treated unfairly. She was not the first black ever to refuse to give up her seat. But her action had unprecedented consequences. King and other black leaders started a boycott of Montgomery's buses; it lasted for 382 days, with blacks walking, cycling or going by mule instead. Other cities followed suit. Mrs Parks's case went to the Supreme Court, which ruled that bus segregation was illegal. Most important, a movement of non-violent protest had begun, with King as its extraordinary spokesman, which eventually recruited the courts, the president and Congress to the cause of equal rights. And Mrs Parks, small, pretty, bespectacled and soft-spoken, was seen as its instigator.

The Klansmen riding

Racism had tainted her life from the beginning. On her grandparents' farm at Pine Level, in the Alabama wilds, she attended for a while a one-room school for blacks only; classes lasted only five months, to release the children for work in the fields. At night she sometimes heard lynchings, and the Klansmen riding. Once the body of a young black was found in the woods; no one knew who had killed him.

Her later schooling was cut short by the need to care for her sick grandmother. She took in sewing, learned typing, married young, but also got involved in black politics. In the Montgomery Voters' League, she helped would-be voters weave their way through the Jim Crow tests designed to keep them from the ballot, and tried several times to register to vote herself. She also joined the National Association for the Advancement of Coloured People (NAACP), becoming secretary of the Montgomery chapter in 1943. Long preparation, therefore, preceded her act of defiance.

Yet life in the South became too hard for her after the boycott. Fired from her job, she left for Detroit in 1957, the destination in those days of thousands of other poor blacks. She was still no celebrity, and continued to take in sewing. Eventually, a local black congressman, John Conyers, hired her to manage his office. She raised funds for the NAACP, appeared at events alongside King, and slowly came to realise that she was an inspiration. In 1999 she was given a Congressional Gold Medal of Honour, the highest honour possible for an American civilian.

As she grew older she was asked, often and almost obsessively, how much race relations had truly improved in America since the passing of the civil-rights laws. She thought there was still far to go. In 1994 she was beaten and robbed by a young black high on drugs and alcohol and fuelled, she supposed, by frustrations much like her own. Although he knew who she was, he said it made no difference to him.

In 1987 she had founded the Rosa and Raymond Parks Institute for Self-Development which, as one of its programmes, took children of different races round the country to learn about the civil-rights movement. They travelled by bus, naturally, sitting where they pleased. By this time, the famous green, white and yellow bus on which she herself had sat, unmoving, had become an exhibit at the Henry Ford Museum in Dearborn, Michigan. But Mrs Parks was well aware that the journey she had started that day was unfinished.

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Overview

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New figures this week suggest that the euro area economies may be turning the corner. **Germany's** IFO index of business confidence jumped from 96 in September to 98.7 in October, its highest level for five years. There was a particularly sharp rise in confidence in the retail sector, suggesting that domestic demand is picking up. In the same month, **French** business confidence rose to an eight-month high and **Italian** business confidence hit an 11-month high.

Largely as a result of dearer oil imports, the **euro area's** current-account surplus narrowed to only $6 billion in the 12 months to August, from $60 billion in the year to August 2004.

Retail sales in **Japan** rose by 1.9% in the year to August, compared with a decline of 1.2% a year earlier.

Britain's GDP growth has halved over the past year, to 1.6% in the year to the third quarter. Record debt levels are putting a strain on households: mortgage repossession orders surged by 66% in the year to the third quarter, to their highest for nine years.

Germany's inflation rate fell to 2.4% in October from 2.5% in September. In the year to August, German workers' average wages rose by only 0.9%, implying a 1% drop in real pay. By contrast, real wages in **Italy** rose by 1.1% in the year to September.

Sales of existing homes in **America** remained unchanged in September from a month earlier—stronger than expected and the second highest on record. Median house prices were 13.4% up on a year ago. However, mortgage applications fell to a six-month low last week. The interest rate on 30-year mortgage rates has risen to 6.1%, from 5.5% in June. The Conference Board's index of consumer confidence fell again in October.

Canada's 12-month rate of consumer-price inflation jumped to 3.4% in September, from 2.6% in August, mainly due to a surge in oil prices. The core inflation rate (excluding food and energy) remained unchanged at 1.7%. Consumer-price inflation in **Australia** rose to 3.0% in the third quarter from 2.5% in the second, lifting the rate to the ceiling of the Reserve Bank's target.

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Output, demand and jobs

Oct 27th 2005
From The Economist print edition

% change on year ago

	GDP		The Economist poll GDP forecasts		Industrial production		Retail sales (volume)		Unemployment % rate	
	latest	qtr*	2005	2006	latest		latest		latest	year ago
Australia	+ 2.6 Q2	+ 5.2	+ 2.6	+ 3.3	+ 0.7	Q2	+ 1.6	Q2	5.1 Sep	5.5
Austria	+ 2.1 Q2	+ 1.8	+ 1.8	+ 2.0	+ 5.4	Jul	– 1.5	Jul	5.2 Sep	4.9
Belgium	+ 1.1 Q3	+ 1.6	+ 1.3	+ 1.7	– 2.3	Aug	+ 6.7	Jul	13.5 Sep†	13.2
Britain	+ 1.6 Q3	+ 1.6	+ 1.9	+ 2.1	– 1.9	Aug	+ 0.7	Sep	4.7 Aug††	4.7
Canada	+ 2.7 Q2	+ 3.2	+ 2.9	+ 3.0	+ 0.6	Jul	+ 6.7	Jul	6.7 Sep	7.0
Denmark	+ 4.3 Q2	+ 6.6	+ 2.0	+ 2.1	+ 0.1	Aug	+ 4.9	Aug	5.7 Aug	6.4
France	+ 1.3 Q2	+ 0.5	+ 1.4	+ 1.6	+ 2.0	Aug	+ 4.1	Aug	9.9 Aug	10.0
Germany	+ 0.6 Q2	nil	+ 0.9	+ 1.1	+ 2.1	Aug	+ 2.2	Aug	11.7 Sep§	10.7
Italy	+ 0.1 Q2	+ 2.7	nil	+ 0.9	+ 6.1	Aug	– 1.6	Jul	7.7 Jun	8.1
Japan	+ 1.4 Q2	+ 3.3	+ 2.2	+ 2.0	+ 1.5	Aug	+ 1.9	Aug	4.3 Aug	4.8
Netherlands	+ 1.3 Q2	+ 4.9	+ 0.6	+ 1.6	– 0.3	Aug	+ 0.7	Jul	6.6 Sep**	6.1
Spain	+ 3.4 Q2	+ 3.4	+ 3.3	+ 2.9	+ 3.8	Aug	+ 3.1	Aug	9.4 Aug	10.8
Sweden	+ 2.3 Q2	+ 2.6	+ 2.3	+ 2.7	– 4.0	Aug	+ 6.5	Sep	5.4 Sep†	5.8
Switzerland	+ 1.0 Q2	+ 1.1	+ 1.1	+ 1.6	+ 3.9	Q2	+ 4.7	Aug	3.6 Sep†	3.7
United States	+ 3.6 Q2	+ 3.3	+ 3.5	+ 3.2	+ 2.0	Sep	+ 5.0	Aug	5.1 Sep	5.4
Euro area	+ 1.1 Q2	+ 1.2	+ 1.2	+ 1.5	+ 2.6	Aug	+ 2.0	Aug	8.6 Aug	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*									
Finland	+ 0.2 Q2	– 6.3	na	na	– 3.9	Aug	+ 5.8	Aug	8.3 Sep†	8.4
Greece	+ 3.7 Q2	na	na	na	+ 1.4	Aug	+ 4.0	Jul	9.9 Mar	10.8
Iceland	+ 6.8 Q2	na	na	na	na		na		1.8 Aug†	2.9
Ireland	+ 4.1 Q2	+ 6.5	na	na	+16.6	Aug	+ 4.2	Aug	4.4 Sep	4.4
Luxembourg	+ 3.1 Q1	na	na	na	+15.7	Jul	– 4.4	Aug	4.5 Aug	4.0
New Zealand	+ 2.6 Q2	+ 4.5	na	na	+ 3.5	Q4	+ 5.9	Q2	3.7 Q2	4.0
Norway	+ 4.8 Q2	+ 5.2	na	na	+ 9.5	Aug	+ 5.1	Aug	4.8 Aug‡	4.5
Portugal	+ 0.5 Q2	+ 4.1	na	na	– 0.8	Jul	+ 1.4	Aug	7.2 Q2†	6.3

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††Jun-Aug; claimant count rate 2.8% in Sep.
§EU harmonised rate 9.3% in Aug. **Jul-Sep.

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Prices and wages

Oct 27th 2005
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2005	2006	latest		year ago	latest		year ago
Australia	+ 3.0	Q3	+ 2.3	+ 2.6	+ 2.7	+ 6.2	Q3	+ 6.1	+ 5.8	Q2	+ 3.0
Austria	+ 2.4	Sep	+ 2.1	+ 2.2	+ 2.0	+ 1.5	Sep	+ 6.0	+ 2.3	Sep	+ 2.0
Belgium	+ 3.2	Sep	+ 2.0	+ 2.5	+ 2.2	+ 1.5	Sep	+ 6.0	+ 2.5	Jul	+ 2.2
Britain	+ 2.5	Sep*	+ 1.1	+ 2.1	+ 2.2	+ 3.3	Sep	+ 3.1	+ 4.2	Aug†	+ 3.8
Canada	+ 3.4	Sep	+ 1.8	+ 2.3	+ 2.4	– 0.4	Aug	+ 5.5	+ 1.4	Jul	+ 1.5
Denmark	+ 2.4	Sep	+ 1.1	+ 1.6	+ 1.9	+ 5.3	Sep	+ 3.4	+ 2.9	Q2	+ 3.1
France	+ 2.2	Sep	+ 2.1	+ 2.0	+ 1.7	+ 2.8	Aug	+ 2.8	+ 2.9	Q2	+ 2.8
Germany	+ 2.4	Oct	+ 2.0	+ 1.9	+ 1.8	+ 3.6	Sep	+ 3.4	+ 0.9	Aug	+ 1.6
Italy	+ 2.0	Sep	+ 2.1	+ 2.2	+ 2.1	+ 3.7	Aug	+ 3.5	+ 3.1	Sep	+ 2.5
Japan	– 0.3	Aug	– 0.2	– 0.1	+ 0.3	+ 1.7	Sep	+ 1.9	– 2.7	Aug	+ 2.8
Netherlands	+ 1.8	Sep	+ 1.0	+ 1.5	na	+ 4.9	Aug	+ 5.5	+ 1.0	Sep	+ 0.9
Spain	+ 3.7	Sep	+ 3.2	+ 3.2	+ 3.1	+ 5.4	Sep	+ 4.6	+ 3.4	Q2	+ 3.1
Sweden	+ 0.6	Sep	+ 0.6	+ 0.7	+ 1.5	+ 4.2	Sep	+ 2.1	+ 2.5	Jul	+ 3.4
Switzerland	+ 1.4	Sep	+ 0.9	+ 1.2	+ 1.2	+ 1.5	Sep	+ 1.5	+ 0.9	2004	+ 1.4
United States	+ 4.7	Sep	+ 2.5	+ 3.2	+ 3.0	+ 6.7	Sep	+ 3.3	+ 2.6	Sep	+ 2.4
Euro area	+ 2.6	Sep	+ 2.1	+ 2.2	+ 1.9	+ 4.0	Aug	+ 3.1	+ 2.3	Q2	+ 2.1
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.2	Sep	+ 0.4	na	na	+ 3.8	Sep	+ 2.5	+ 4.0	Q2	+ 3.8
Greece	+ 3.9	Sep	+ 2.7	na	na	+ 5.5	Aug	+ 4.9	na		na
Iceland	+ 4.6	Oct	+ 3.7	na	na	+ 4.6	Sep	+ 5.2	+ 6.7	Aug	+ 5.2
Ireland	+ 3.0	Sep	+ 2.5	na	na	– 1.1	Aug	– 0.4	+ 3.4	Q2	+ 4.3
Luxembourg	+ 2.9	Sep	+ 2.0	na	na	+ 4.1	Aug	+11.3	+ 0.7	Jul	+ 2.2
New Zealand	+ 3.4	Q3	+ 2.5	na	na	+ 4.7	Q2	+ 1.5	+ 2.6	Q2	+ 2.3
Norway	+ 2.0	Sep	+ 1.1	na	na	+17.9	Sep	+20.3	+ 3.8	Q2	+ 4.1
Portugal	+ 2.8	Sep	+ 2.1	na	na	+ 4.5	Sep	+ 4.5	nil	Aug	– 2.2

*RPI inflation rate 2.7% in Sep. †Jun-Aug.

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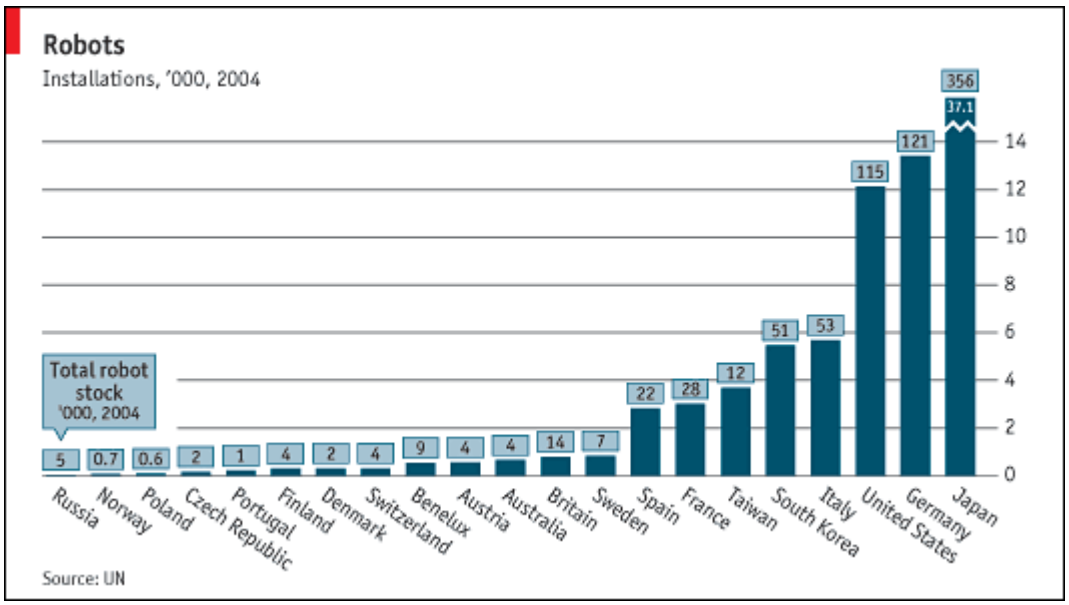
Robots

Oct 27th 2005
From The Economist print edition

Robots are coming back into fashion. Worldwide sales of multipurpose, industrial robots grew by 17% in volume last year, according to a joint survey by the International Federation of Robotics and the United Nations. Japan has over 350,000 robots in operation, the world's biggest stock. But Europe is catching up. In 1994, Europe had only a third as many robots as Japan. Ten years later, it had three-quarters as many.



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Money and interest rates

Oct 27th 2005
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Oct 26th 2005)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 5.6	+ 8.6	Aug	5.66	5.44	5.33	5.48	5.30	6.47
Britain	+ 5.4	+11.2	Sep	4.53	4.84	4.31	4.42	4.68	5.17
Canada	+ 7.4	+ 9.7	Aug	3.03	2.57	3.60	4.15	4.45	5.30
Denmark	+22.8	+16.3	Sep	2.25	2.25	2.43	3.30	3.86	4.92
Japan	+ 5.2	+ 2.1	Sep	0.02	0.03	0.27	1.55	1.42	1.59
Sweden	+ 2.5	+ 6.2	Aug	1.46	1.99	2.14	3.22	4.10	3.03
Switzerland	+ 3.2	+ 6.3	Sep	0.83	0.71	1.47	1.92	2.43	2.12
United States	+ 0.3	+ 6.6	Sep	4.17	2.06	4.38	4.59	3.99	5.47
Euro area†	+11.5	+ 8.1	Aug	2.21	2.15	2.54	3.34	3.78	3.67

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. Benchmarks: US 30-year 4.80%, Japan No. 273 1.55%. Central bank rates: US fed funds 3.75%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Oct 27th 2005
From The Economist print edition

2000=100

	Oct 18th	Oct 25th*	% change on one month	% change on one year
Dollar index				
All items	136.3	135.1	+ 2.3	+12.4
Food	124.8	124.4	+ 3.0	+ 8.8
Industrials				
All	151.2	149.0	+ 1.6	+16.6
Nfa†	136.0	135.2	+ 1.4	+10.3
Metals	159.5	156.6	+ 1.7	+19.8
Sterling index				
All items	118.3	114.8	+ 1.2	+15.7
Euro index				
All items	105.7	103.3	+ 1.5	+18.7
Yen index				
All items	146.5	143.8	+ 3.5	+20.9
Gold				
$ per oz	472.50	472.30	+ 2.7	+10.9
West Texas Intermediate				
$ per barrel	63.03	62.32	– 4.2	+12.9

* Provisional. † Non-food agriculturals.

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Stockmarkets

Oct 27th 2005
From The Economist print edition

Market indices

	Oct 26th	2005 high	2005 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,400.6	4,617.4	3,905.5	+ 1.3	- 4.7	+ 8.6	+ 4.5
Austria (ATX)	3,195.2§	3,503.9	2,415.0	+ 1.3	- 8.8	+31.4	+16.8
Belgium (Bel 20)	3,265.2	3,373.8	2,958.8	+ 0.8	-11.3	+11.3	- 1.1
Britain (FTSE 100)	5,227.8	5,501.6	4,783.6	+ 1.2	-24.6	+ 8.6	+ 0.4
Canada (Toronto Composite)	10,283.7	11,081.2	9,006.2	- 1.4	- 9.7	+11.2	+14.0
Denmark (OMXCB)	327.5	341.9	257.8	+ 2.2	- 4.2	+27.0	+12.6
France (SBF 250)	3,080.9	3,248.3	2,633.6	+ 1.0	-29.8	+17.0	+ 3.9
(CAC 40)	4,412.7	4,650.2	3,816.1	+ 0.9	-36.3	+15.5	+ 2.6
Germany (DAX)*	4,900.8	5,138.0	4,178.1	+ 1.1	-39.2	+15.1	+ 2.3
Italy (S&P/MIB)	32,827.0	34,874.0	30,645.0	+ 1.7	-34.5	+ 6.2	- 5.6
Japan (Nikkei 225)	13,395.0	13,738.8	10,825.4	+ 2.0	-65.6	+16.6	+ 3.2
(Topix)	1,407.7	1,428.1	1,109.2	+ 2.0	-51.2	+22.4	+ 8.4
Netherlands (AEX)	390.7	408.7	347.0	+ 0.9	-44.3	+12.2	- 0.3
Spain (Madrid SE)	1,128.4	1,176.9	950.9	+ 0.8	- 4.1	+17.7	+ 4.5
Sweden (Affarsvarlden Gen)	263.9	273.7	218.9	+ 1.9	-34.1	+19.3	+ 0.7
Switzerland (Swiss Market)	6,972.4	7,042.3	5,669.6	+ 2.2	-17.1	+22.5	+ 8.7
United States (DJIA)	10,345.0	10,940.6	10,012.4	- 0.7	-11.8	- 4.1	- 4.1
(S&P 500)	1,191.4	1,245.0	1,137.5	- 0.4	-22.0	- 1.7	- 1.7
(NASDAQ Comp)	2,100.1	2,218.2	1,904.2	+ 0.4	-58.4	- 3.5	- 3.5
Europe (FTSEurofirst 300)†	1,186.6	1,242.0	1,038.6	+ 1.2	-30.4	+13.9	+ 1.2
Euro area (FTSE Euro 100)†	1,006.9	1,056.1	894.4	+ 0.8	-35.1	+11.8	- 0.7
World (MSCI)‡	1,182.9	1,225.6	1,115.0	+ 0.7	-18.4	+ 1.2	+ 1.2
World bond market (Citigroup)††	624.0	662.3	621.5	- 0.1	- 5.8	- 6.3	- 6.3

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms. §Oct 25th.

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Trade, exchange rates and budgets

Oct 27th 2005
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Oct 26th	year ago	Currency units per $ Oct 26th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 16.4	Aug	− 43.1	Q2	− 4.8	− 4.4	118.4	112.5	1.33	1.34	2.35	1.60	1.14	+ 0.9
Austria	− 1.2	Aug	− 0.3	Aug	− 0.4	− 0.6	104.1§	103.9	0.83	0.78	1.47	–	0.72	− 2.0
Belgium	+ 16.3	Aug	+ 9.2	Jun	+ 2.8	+ 2.7	104.7§	104.4	0.83	0.78	1.47	–	0.72	− 0.5
Britain	−115.6	Aug	− 23.5	Q2	− 2.4	− 2.5	99.3	99.0	0.56	0.54	–	0.68	0.49	− 2.9
Canada	+ 45.6	Aug	+ 16.3	Q2	+ 1.6	+ 1.5	124.1	117.4	1.17	1.22	2.08	1.41	1.01	+ 1.2
Denmark	+ 9.9	Aug	+ 9.7	Aug	+ 2.9	+ 2.7	106.0	106.4	6.18	5.82	11.0	7.46	5.33	+ 1.8
France	− 27.1	Aug	− 25.9	Aug	− 0.8	− 0.8	107.3§	106.9	0.83	0.78	1.47	–	0.72	− 3.0
Germany	+200.2	Aug	+110.4	Aug	+ 3.7	+ 3.5	105.1§	104.7	0.83	0.78	1.47	–	0.72	− 3.5
Italy	− 8.8	Aug	− 28.5	Aug	− 1.4	− 1.5	76.8§	76.6	0.83	0.78	1.47	–	0.72	− 4.4
Japan	+104.9	Aug	+163.7	Aug	+ 3.4	+ 3.3	82.8	88.3	116	106	206	140	–	− 6.1
Netherlands	+ 40.3	Aug	+ 28.3	Q2	+ 3.7	+ 3.6	104.2§	103.8	0.83	0.78	1.47	–	0.72	− 2.2
Spain	− 92.9	Aug	− 75.9	Jul	− 6.1	− 6.0	77.4§	77.2	0.83	0.78	1.47	–	0.72	+ 0.5
Sweden	+ 21.3	Sep	+ 27.9	Q2	+ 7.1	+ 6.6	94.3	100.4	7.87	7.06	14.0	9.51	6.80	+ 0.8
Switzerland	+ 7.2	Sep	+ 51.4	Q2	+11.4	+10.9	106.8	108.4	1.28	1.20	2.28	1.55	1.11	− 1.0
United States	−737.4	Aug	−749.7	Q2	− 6.5	− 6.6	86.3	83.0	–	–	1.78	1.21	0.86	− 4.1
Euro area	+ 49.4	Aug	+ 6.0	Aug	+ 0.2	+ 0.2	116.0	117.7	0.83	0.78	1.47	–	0.72	− 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 11.4	Aug	+ 7.7	Aug	na	na	81.7§	81.5	0.83	0.78	1.47	–	0.72	+ 1.3
Greece	− 33.8	Aug	− 16.2	Aug	na	na	60.0§	59.9	0.83	0.78	1.47	–	0.72	− 3.8
Iceland	− 1.1	Aug	− 1.6	Q2	na	na	105.1**	95.9	60.4	69.1	107	73.0	52.2	+ 1.1
Ireland	+ 40.3	Aug	− 3.9	Q2	na	na	94.6§	93.9	0.83	0.78	1.47	–	0.72	− 0.7
Luxembourg	− 4.4	Jul	+ 3.5	Q2	na	na	104.7§	104.4	0.83	0.78	1.47	–	0.72	− 0.8
New Zealand	− 4.0	Aug	− 8.2	Q2	na	na	140.0	133.9	1.42	1.43	2.52	1.72	1.23	+ 3.2
Norway	+ 44.6	Sep	+ 40.8	Q2	na	na	112.2	107.1	6.47	6.39	11.5	7.81	5.59	+ 14.4
Portugal	− 14.0	Jul	− 16.5	Aug	na	na	93.4**	93.4	0.83	0.78	1.47	–	0.72	− 5.3

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, August average. ‡OECD forecast. **IMF, June average.

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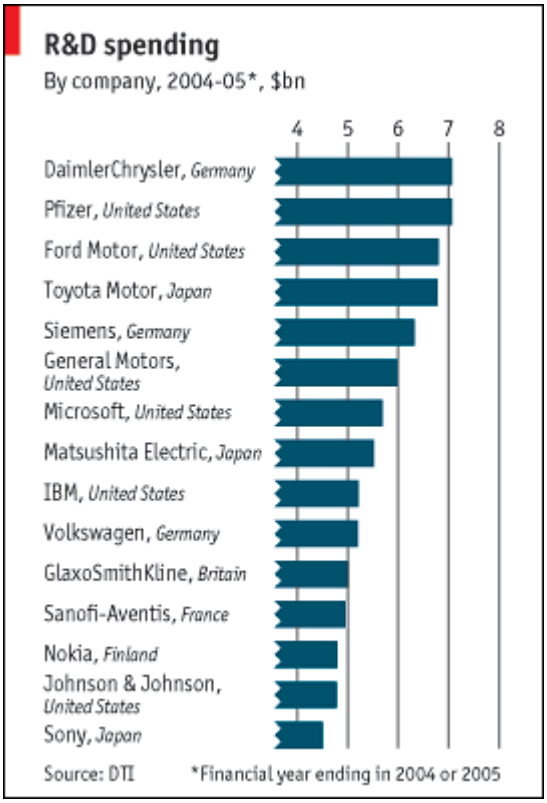
R&D spending

Oct 27th 2005
From The Economist print edition



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Overview

Oct 27th 2005
From The Economist print edition

Industrial production is growing briskly in many parts of Asia. In the year to August, it expanded by 7.4% in Indonesia and by 7.3% in the Philippines. In the year to September, it grew by 6.2% in Taiwan and by a prodigious, and unexpected, 21.1% in Singapore.

The **Reserve Bank of India**, the country's central bank, raised its key interest rate by 0.25% to 5.25%, to head off the inflationary threat posed by higher oil prices.

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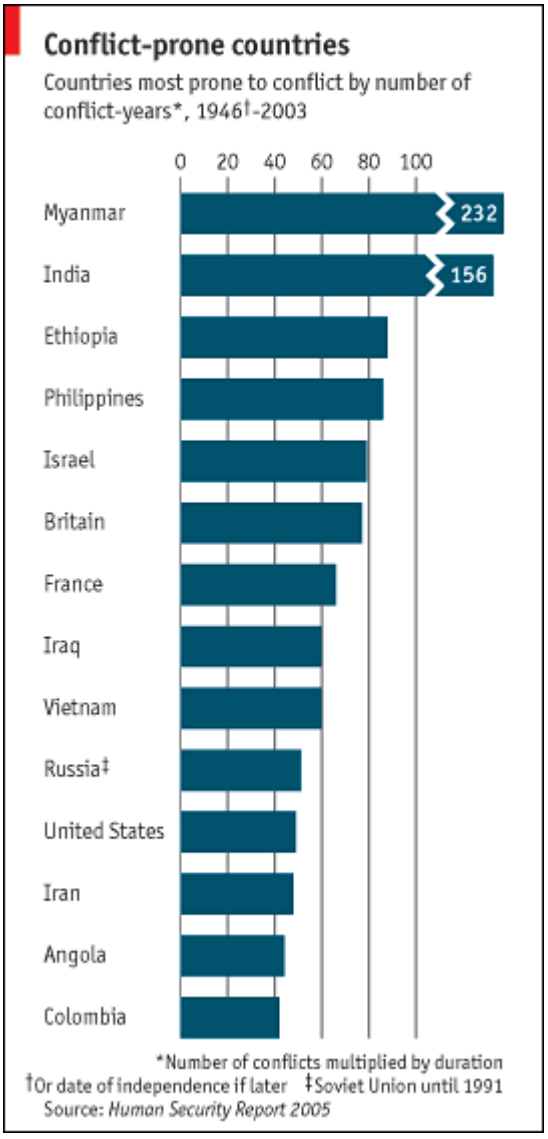
Conflict-prone countries

Oct 27th 2005
From The Economist print edition

In 2003, governments fought 29 armed conflicts, down from over 50 in 1992, according to the *Human Security Report* which draws on research by Sweden's Uppsala University and the International Peace Research Institute in Oslo. Between 1989 and 2002, about 100 conflicts came to an end. Indeed, fewer people were killed in battle in the 1990s than in any other post-war decade. Which states are most prone to conflict? One ranking counts both the number of conflicts and their length. A single war lasting five years is equivalent to five wars of a year each. By this measure, Myanmar, which waged six internal conflicts in the 1960s, tops the list, while India, long-mired in a violent dispute over Kashmir, is second.



Economy

Oct 27th 2005
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.4	Q3	+16.5	Sep	+ 0.9	Sep	+96.4	Sep	+68.7	2004	769.0	Sep
Hong Kong	+ 6.8	Q2	– 0.1	Q2	+ 1.6	Sep	– 9.5	Sep	+21.3	Q2	122.3	Sep
India	+ 8.1	Q2	+ 7.4	Aug	+ 3.4	Aug	–35.5	Sep	–16.0	Q2	132.2	Sep
Indonesia	+ 5.5	Q2	+ 7.4	Aug	+ 9.1	Sep	+27.2	Aug	+ 4.0	Q2	29.9	Aug
Malaysia	+ 4.1	Q2	+ 4.1	Aug	+ 3.4	Sep	+24.1	Aug	+18.0	Q2	79.5	Aug
Philippines	+ 4.8	Q2	+ 7.3	Aug	+ 7.0	Sep	– 1.3	Aug	+ 3.2	Jun	16.0	Sep
Singapore	+ 6.0	Q3	+21.1	Sep	+ 0.6	Sep	+16.8	Sep	+32.5	Q2	115.6	Sep
South Korea	+ 3.3	Q2	+ 5.5	Aug	+ 2.7	Sep	+25.2	Sep	+18.6	Sep	206.7	Sep
Taiwan	+ 3.0	Q2	+ 6.2	Sep	+ 3.1	Sep	+ 1.7	Sep	+13.3	Q2	253.8	Sep
Thailand	+ 4.4	Q2	+10.7	Aug	+ 6.0	Sep	– 7.3	Aug	– 2.3	Aug	48.2	Aug
Argentina	+10.1	Q2	+ 6.0	Aug	+10.3	Sep	+11.4	Aug	+ 2.9	Q2	24.8	Sep
Brazil	+ 3.9	Q2	+ 3.8	Aug	+ 6.0	Sep	+41.2	Sep	+12.5	Aug	54.6	Aug
Chile	+ 6.5	Q2	+ 4.5	Aug	+ 3.9	Sep	+ 8.9	Sep	+ 0.6	Q2	15.7	Sep
Colombia	+ 5.3	Q2	– 0.2	Jul	+ 5.0	Sep	+ 1.7	Jul	– 0.8	Q2	14.8	Sep
Mexico	+ 3.1	Q2	+ 2.1	Aug	+ 3.5	Sep	– 9.5	Aug	– 8.4	Q2	68.2	Aug
Peru	+ 6.7	Aug	+ 9.4	Aug	+ 1.1	Sep	+ 4.1	Aug	+ 0.4	Q2	12.8	Sep
Venezuela	+11.1	Q2	+ 8.0	Jul	+15.9	Sep	+24.7	Q2	+17.7	Q2	24.7	Jul
Egypt	+ 5.2	Q1	+ 3.3	2004†	+ 4.7	Aug	–10.4	Q2	+ 2.9	Q2	19.0	Aug
Israel	+ 4.8	Q2	+ 3.6	Jul	+ 1.9	Sep	– 8.3	Sep	+ 1.3	Q2	28.5	Sep
South Africa	+ 4.5	Q2	+ 3.5	Aug	+ 4.4	Sep	– 2.4	Aug	– 8.6	Q2	17.6	Sep
Czech Republic	+ 5.1	Q2	+ 8.6	Aug	+ 2.2	Sep	+ 1.4	Aug	– 4.1	Q2	29.9	Sep
Hungary	+ 4.1	Q2	+ 6.9	Aug	+ 3.7	Sep	– 3.5	Aug	– 8.6	Q2	17.5	Sep
Poland	+ 2.8	Q2	+ 5.5	Sep	+ 1.8	Sep	– 3.6	Aug	– 0.5	Aug	39.9	Aug
Russia	+ 6.1	Q2	+ 5.2	Sep	+12.4	Sep	+113.4	Aug	+78.3	Q2	159.6	Sep
Turkey	+ 4.2	Q2	+ 8.3	Aug	+ 8.0	Sep	–40.4	Aug	–20.7	Aug	41.2	Aug
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 9.9	Q2	+ 5.5	Aug	+ 4.9	Sep	– 2.4	Aug	– 1.4	Aug	1.8	Aug
Latvia	+11.6	Q2	+ 8.9	Aug	+ 7.2	Sep	– 2.8	Aug	– 1.7	Aug	2.2	Aug
Lithuania	+ 8.0	Q2	na		+ 2.6	Sep	– 3.2	Aug	– 1.5	Aug	3.5	Aug
Slovakia	+ 5.1	Q2	+ 4.3	Aug	+ 2.2	Sep	– 1.9	Aug	– 2.4	Jun	15.4	Aug
Slovenia	+ 5.2	Q2	+ 1.4	Aug	+ 3.2	Sep	– 1.3	Aug	+ 0.2	Aug	8.1	Jun
Pakistan	+ 8.4	2005†	+13.6	Apr	+ 8.5	Sep	– 7.9	Sep	– 1.5	Q2	10.2	Sep
Saudi Arabia	+ 6.2	2005	na		+ 0.3	Jul	+85.2	2004	+51.5	2004	24.8	Aug

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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Financial markets

Oct 27th 2005
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% charige on		
	per $		per £	short-term	Oct 26th		Dec 31st 2004	
	Oct 26th	year ago	Oct 26th	% a year		one week	in local currency	in $ terms
China	8.09	8.28	14.4	2.00	1,153.4	-3.3	- 13.3	- 11.3
Hong Kong	7.75	7.78	13.8	4.27	14,458.1	+0.6	+ 1.6	+ 1.9
India	45.0	45.6	80.0	5.47	7,974.7	nil	+ 20.8	+ 16.6
Indonesia	9,992	9,112	17,745	14.00	1,062.2	-1.3	+ 6.2	- 1.3
Malaysia	3.77	3.80	6.70	2.94	905.2	-1.0	- 0.2	+ 0.4
Philippines	55.0	56.4	97.7	8.13	1,934.6	-1.0	+ 6.1	+ 8.3
Singapore	1.69	1.66	3.01	2.44	2,228.8	+0.5	+ 7.9	+ 4.0
South Korea	1,046	1,125	1,857	3.89	1,179.0	+2.2	+ 31.6	+ 30.3
Taiwan	33.7	33.6	59.8	1.55	5,700.7	+0.1	- 7.1	- 12.6
Thailand	40.8	41.1	72.5	4.25	685.0	+0.1	+ 2.5	- 2.5
Argentina	2.99	2.97	5.32	6.88	1,609.8	+0.5	+ 17.0	+ 16.2
Brazil	2.27	2.86	4.03	18.95	29,728.7	+1.5	+ 13.5	+ 32.8
Chile	547	611	971	4.32	9,893.5	-1.1	+ 10.4	+ 12.2
Colombia	2,288	2,576	4,063	6.45	7,070.0	+0.6	+ 62.7	+ 67.3
Mexico	10.9	11.5	19.3	8.82	15,666.2	+3.7	+ 21.3	+ 24.1
Peru	3.39	3.32	6.02	2.99	5,001.9	+1.0	+ 34.8	+ 30.4
Venezuela	2,834§	2,491§	5,033	11.68	19,440.1	-4.6	- 35.1	- 41.0
Egypt	5.76	6.22	10.23	9.32	47,735.6	-0.7	+ 94.2	+104.5
Israel	4.63	4.46	8.22	4.07	759.7	+3.2	+ 18.0	+ 10.2
South Africa	6.69	6.15	11.9	7.25	16,442.7	+5.8	+ 29.9	+ 9.4
Czech Republic	24.7	24.7	43.8	1.97	1,348.2	+3.0	+ 30.6	+ 18.3
Hungary	209	193	371	6.24	20,796.1	+5.5	+ 41.1	+ 22.0
Poland	3.29	3.39	5.85	4.53	31,987.0	+2.3	+ 20.1	+ 9.2
Russia	28.5	28.8	50.6	13.00	910.4‡	+3.2	+ 52.4	+ 48.3
Turkey	1.36	1.48	2.41	15.63	31,474.4	+2.3	+ 26.0	+ 25.4
EM (MSCI)*	1.00	1.00	1.78	na	615.6	+2.0	+ 13.5	+ 13.5
EMBI+†	1.00	1.00	1.78	na	353.1	+0.1	+ 7.2	+ 7.2

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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